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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-1543

M. M. HARDIN, AKSEL NIELSEN, D. W. REEVES, J. EARLE MAY, ALBERT W. THOMSON, R. C. SCHENK, A.D. MARTIN, and H.F. KORHOLZ,

Petitioners,

v.

MARY M. DASHO, Executor for the Estate of William A. Dasho, Deceased, DASHO-ROGERS, INC., an Illinois corporation, and MAURICE H. SCHY,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The Petitioners* respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered in this proceeding on January 18, 1972.

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*Of the defendants below, The Susquehanna Corporation and American Gypsum Company will file a separate petition, as will Edward O. Boshell, Ralph A.L. Bogan, Harold C. Stuart and Francis M. Woolard. For this reason, these parties are not named as Petitioners.

OPINIONS BELOW

The opinion of the Court of Appeals, not yet reported, appears in the Appendix hereto. The opinion of the District Court for the Northern District of Illinois, not yet reported, also appears in the Appendix hereto.

JURISDICTION

The judgment of the Court of Appeals for the Seventh Circuit was entered on January 18, 1972. A timely petition for rehearing *en banc* was denied on February 25, 1972, and this petition for certiorari was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. §1254 (1).

STATUTORY PROVISIONS INVOLVED

Section 10 (b), Securities and Exchange Act of 1934, 15 U.S.C. §78j(b) and Securities and Exchange Commission Rule 10b-5, 17 C.F.R. §240, 10b-5, are contained in the Appendix hereto.

QUESTIONS PRESENTED

1. Whether the rule of *Ross v. Bernhard* is to be given retroactive application to stockholders' derivative suits which have been tried to the court prior to that decision.

2. Whether the Seventh Amendment right of jury trial has been improperly extended by the Seventh Circuit beyond the rule of *Ross v. Bernhard* to claims based upon fraud and breach of fiduciary duty.

3. Where the case was closed at the end of Plaintiffs' evidence and the District Court's decision and findings for Defendants clearly establish that the case would have been taken from a jury, should the case be remanded for a jury trial?

STATEMENT OF THE CASE

This action was initiated in the United States District Court for the Northern District of Illinois on October 22, 1965 by shareholders of Susquehanna Corporation for the purposes of preventing the consummation of a merger of Susquehanna and American Gypsum Company and of recovering damages for certain transactions engaged in by the Board of Directors. It was a two-count action arising under the Securities Act of 1933 and the Securities Exchange Act of 1934, charging conspiracy. It was alleged that Susquehanna would be harmed not only by the merger but also by an earlier purchase of its own shares at an unfair price. The District Court refused to enjoin the merger and dismissed the counts based on Section 17 (a) of the Securities Act of 1933, 15 U.S.C. §77 q(a) and Section 10(b) of the Securities Act of 1934, 15 U.S.C. §78j (b), and Rule 10b-5 thereunder, for want of standing and jurisdiction. On appeal from the order of dismissal, the Court of Appeals held, in substance, that a merger constitutes a sale within the meaning of Rule 10b-5 promulgated pursuant to Section 10(b) of the Securities Exchange Act of 1934, that requisite standing and jurisdiction existed. It remanded the case for trial. *Dasho v. Susquehanna Corp.*, 380 F.2d 262 (7th Cir. 1967), *cert. denied sub nom., Bard v. Dasho*, 389 U.S. 977 (1967).

Upon remand, amendments to the pleadings were filed, extensive discovery was conducted, plaintiffs voluntarily dismissed three defendants,[1] and a non-jury trial was held between September 17 and October 22, 1969. At the completion of the five-week trial, defendants rested their case without the necessity of having to call any witnesses. Plaintiffs clearly made defendants' case for them.

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[1] At the opening of trial, Respondents dismissed from the case three defendants. The dismissal of the claims against defendants J. Patrick Lannan, Howard J. Lauhoff and Franklin B. Schmick was affirmed by the Court of Appeals. Defendant Hugh C. Michels died pending appeal and the dismissal as to him was also affirmed. See p. 32a, Appendix hereto.

After the trial, plaintiffs filed a complaint to conform their final theories of the case to the proof. In that pleading they abandoned all charges of conspiracy. The District Court entered extensive findings of fact, conclusions of law and a judgment for the defendants on all claims.

A jury demand, which the Court of Appeals found sufficient to entitle plaintiffs to a jury trial, was filed on December 30, 1968, some 38 months after the filing of the original complaint, several months after all defendants had answered, and was incorporated in a reply which itself was not filed within the specified time. It was endorsed on plaintiff's Reply to certain affirmative defenses filed by only three of the 18 defendants who were parties to the action. As a reply to affirmative defenses, it was a superfluous pleading since it was no more than a denial of allegations already in issue.

Prior to the trial, the trial court struck the jury demand relying on the opinion of the Court of Appeals for the Second Circuit in *Ross v. Bernhard,* 403 F.2d 909 (2d Cir. 1969). After the trial this Court announced its decision in *Ross v. Bernhard*, 396 U.S. 531 (1970). In post trial proceedings, the trial court declined to apply the *Ross* decision retroactively. The trial court also questioned the timeliness of the jury demand. Finding that the jury demand was timely, that it should apply to all defendants, and that based on *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971), *Ross v. Bernhard* should be retroactively applied in this case, the Court of Appeals reversed in part and remanded for a jury trial.

REASONS FOR GRANTING THE WRIT

1. THE COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW, CONCERNING THE RETROSPECTIVE APPLICATION OF ROSS v. BERNHARD, 396 U.S. 531 (1970), WHICH HAS NOT BEEN BUT SHOULD BE, SETTLED BY THIS COURT.

After the trial to the Court in the instant case, and prior to the Court of Appeals decision, this Court decided *Ross v. Bernhard,* 396 U.S. 531 (1970). That case announced the principle that parties in a stockholder's derivative suit were entitled to a jury trial on those issues as to which the corporation, had it been suing in its own right, would have been entitled to a jury. Prior to that decision, the historic rule was that such a suit could be brought only in equity.

In the instant case, the Court of Appeals, in rather summary fashion held that decision to be retrospective and reversed and remanded the case for a jury trial. See pp. 11a-13a of Appendix hereto.

In so doing, the Court of Appeals has misconstrued and misapplied this Court's opinions in *Linkletter v. Walker,* 381 U.S. 618 (1965), *Johnson v. New Jersey,* 384 U.S. 719 (1966), *DeStefano v. Woods,* 392 U.S. 631 (1968) (per curiam), *Williams v. U.S.,* 401 U.S. 646 (1971), and *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971). These cases all considered the question of whether a judicial decision overturning previously established law should be given retroactive or prospective application.

In *Linkletter,* the touchstone decision on this basic question, the conclusion was reached that "the accepted rule today is that in appropriate cases the Court may in the interest of justice make the rule prospective," and that "we believe that the Constitution neither prohibits nor requires retrospective effect." *Linkletter v. Walker,* 381 U.S. 618, 628, 629 (1965).

In *Johnson v. New Jersey,* 389 U.S. 719 (1966), this Court held that its decisions in *Escobeda v. Illinois,* 378 U.S. 478 (1964) and *Miranda v. Arizona,* 384 U.S. 436 (1966), affected only those cases in which the trial began after the precise date of the respective decisions, and thus would not be retroactively applied to cases still on direct appeal when the decisions were announced. *Williams v. U.S.* 401 U.S. 646 (1971) further held that *Chimel v. California,* 395 U.S. 752 (1969), should not be applied retroactively to the direct review of petitioner's conviction.

In *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971), this Court applied the principles of *Linkletter* and subsequent cases in the criminal area to a non-criminal matter, stating that the Court has "recognized the doctrine of nonretroactivity outside the criminal area many times, in both constitutional and nonconstitutional cases." *Id.* at 106.

And, *DeStefano v. Woods,* 392 U.S. 631 (1968), held that *Duncan v. Louisiana,* 391 U.S. 145 (1968), obligating the states to recognize the right to jury trial in serious criminal cases, and *Bloom v. Illinois,* 391 U.S. 194 (1968), extending the right to jury trial to serious criminal contempts, would receive only prospective application.

Further, the Court in *DeStefano* noted that there was no basis for a distinction between convictions which had become final and cases at various stages of trial and appeal, and stated that it thus would not reverse state convictions for failure to grant jury trial where trials began prior to the date of this Court's decisions in *Duncan v. Louisiana* and *Bloom v. Illinois*. 392 U.S. at 635.

Both *Duncan* and *Bloom* involved the right to jury trial by States by virtue of the Sixth and Fourteenth Amendments, while the instant case involves that right by virtue of the Seventh Amendment. However, the right to a jury trial accorded by the States under the Sixth and Fourteenth Amendments cannot be considered on a lower plane than the right to such trial in civil actions by federal courts by virtue of the Seventh Amendment.

Nonetheless, the Court of Appeals in the instant case gave short shrift to these decisions and the jurisprudential theories underlying them. In dealing with *DeStefano v. Woods, supra,* the Court stated:

> "There is almost no suggestion in any of the cases from *Linkletter v. Walker* . . . , through *Mackey v. United States,* 401 U.S. 667 (See especially Mr. Justice Harlan's concurring opinion, 675-702) that this line of authority should be applied to civil litigation." See pp. 12a, Appendix hereto.

This statement totally ignores the language of *Linkletter v. Walker,* 381 U.S. 618, (1965), itself, to the effect:

> "That no distinction was drawn between civil and criminal litigation is shown by the language used not only in *Schooner Peggy, supra,* [1 Cranch 103 (1801)] and *Chicot County, supra,* [308 U.S. 371 (1940)] but also in such cases as *State v. Jones,* 44

N.M. 623, 107 P.2d 324 (1940) and *James v. United States,* 366 U.S. 213 (1961)." *Id.* at 627.[2]

Although the Court of Appeals noted *Chevron Oil Co.,* it relied upon that case only for the proposition that most *nonretroactive cases have* been in the areas of criminal process, and seemingly ignored the holding otherwise.

Since *Linkletter* this Court has reiterated that there is no inflexible constitutional rule requiring either absolute retroactivity or complete prospectivity, and has not accepted as a dividing line the suggested distinction between cases on direct review and those under collateral attack. *Williams v. U.S.,* 401 U.S. 646, 651 (1971).

Based upon *Linkletter,* the Court has proceeded to:

> "weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." *Linkletter v. Walker, supra,* at 629.

In its summary discussion of the criteria of *Linkletter* and *Chevron,* the Court of Appeals simply stated it was not inequitable to apply *Ross* retroactively, and that it failed to see how retroactive application would retard operation of the rule. See pp. 13a, Appendix hereto.

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[2] See Anno: "United States Supreme Court's View as to the Retroactive Effect of Its Own Decisions Announcing New Rules," 22 L. Ed. 821, 825, stating "[T]he Supreme Court has recognized that in determining the retroactivity of particular new rules, no distinction is to be drawn between civil and criminal litigation, and that with respect to a new constitutional rule the decision as to retroactivity does not depend on the particular constitutional provision on which the rule is based."

This simple disposition of the *Linkletter* criteria fails completely to come to grips with, or even attempt to understand, the philosophy of *Linkletter* and the subsequent cases. The question of nonretroactivity has been considered with respect to a number of cases involving constitutional protections in criminal trials. Where the condemned practice implies a serious flaw in the fact-finding process, retroactivity has been required, but not otherwise. This doctrine was explained in *Williams v. United States,* 401 U.S. 646 (1971) as follows:

> "Where the major purpose of new constitutional doctrine is to overcome an aspect of the criminal trial that substantially impairs its truth-finding function and so raises serious questions about the accuracy of guilty verdicts in past trials, the new rule has been given complete retroactive effect.***"
>
> "It is quite different where the purpose of the new constitutional standard proscribing the use of certain evidence or a particular mode of trial is not to minimize or avoid arbitrary or unreliable results but to serve other ends." *Id.* at653.

In footnote the Court stated:

> "In both *Johnson* and *Stovall,* we frankly acknowledged that '[t]he extent to which a condemned practice infects the integrity of the truth-determining process at trial is a "question of probabilities.'" 388 U.S. at 298. Where we have been unable to conclude that the use of such a 'condemned practice' in past criminal trials presents substantial likelihood that the results of a number of those trials were factually incorrect, we have not accorded retroactive effect to the decision condemning that practice. See, e.g. *DeStefano,* 392, U.S. at 633-634 (quoting Duncan). . . ." *Id.* at 655, n. 7.

The Court of Appeals never discusses these principles in light of the situation in the instant case; *i.e.*, the application of the Seventh Amendment guarantee of jury trial to stockholder derivative suits, which *prescribes* a new mode of trial for such suits. The rule of *Ross* was simply applied retroactively. There is a void in place or reasoned discussion of the philosophy and concept of *Linkletter* and its progeny.

This Court has further clarified the considerations affecting the judgment whether a new standard should be applied retroactively. In *Stovall v. Denno,* 388 U.S. 293, 297 (1967), this Court stated the considerations to be:

> "(a) the purpose to be served by the new standards,
>
> (b) the extent of the reliance by law enforcement authorities on the old standards, and
>
> (c) the effect on the administration of justice of a retroactive application of the new standards."

The language of *DeStefano v. Woods,* 392 U.S. 631, 633 (1969), is particularly applicable here. The Court there held that failure to grant a jury trial does not impair the fact finding process, saying:

> "As we stated in *Duncan,* 'We would not assert, however, that every criminal trial—*or any particular trial*—held before a judge alone is unfair or that a defendant may never be as fairly treated by a judge as he would be by a jury' .... The values implemented by the right to jury trial would not measurably be served by requiring retrial of all persons convicted in the past by procedures not consistent with the Sixth Amendment right to jury trial." (Emphasis added).

DeStefano v. Woods was reaffirmed in *DeBacker v. Brainard,* 396 U.S. 28, 30 (1969) involving the right to trial by jury in a juvenile proceeding.

This reasoning is directly applicable to the instant case. The values implemented by the right to a jury trial would also not be measurably served by requiring retrial of derivative suits which were tried to the court.

As to the second criteria, reliance in the criminal area by States and courts upon previous standards is parallel to that in the civil area. Reliance by a trial court upon a historical standard in holding a non-jury trial lasting for over four weeks cannot be dismissed lightly.

Also, there is no logical basis for a conclusion that a holding extending a constitutional right to trial by jury in criminal cases pursuant to the Sixth Amendment should be nonretroactive, whereas a holding extending the right to trial by jury in civil cases pursuant to the Seventh Amendment should be retroactive.

No rational basis exists for a distinction with respect to criminal cases arising because of a showing of unusual burden on the administration of justice resulting from re-trial problems. "Burden" has not been relied on as a basis for nonretroactivity where, as here, the fact finding process is not in question. It has been heavily relied upon only where the purpose of the rule did not clearly favor either retroactivity or prospectivity. *Desist v. United States,* 394 U.S. 244, 251 (1969).

Even so, here the denial of jury trial in derivative suits has occurred, as in the instant case, in all instances, except *DePinto v. Provident Security Life Ins. Co.,* 323 F.2d 826 (1963). See *DeStefano v. Woods,* 392 U.S. at 634. Retrial of the instant case will undoubtedly involve another four weeks plus trial, further disrupting the district court's already crowded docket. We cannot hazard a guess as to how many other such suits have been tried to the court and are now pending appeal. Retrial of this and similarly situated cases can only have a detrimental effect upon the administration of the courts.

In *Chevron Oil Co. v. Huson,* 404 U.S. 97 (1971), it was held that a state statute of limitations would not be retroactively applied under *Rodreque v. Aetna Casualty & Surety Co.,* 395 U.S. 352 (1969), which held that state law rather than admiralty rules governs actions under the Outer Continental Shelf Lands Act (43 U.S.C. § 1333), where the Plaintiff had sued before the decision but after the expiration of the applicable state limitations period. The tests announced in *Chevron* are not inconsistent with *DeStefano.*

The Court of Appeals, however, in applying the tests stated in *Chevron,* concluded that the decision in *Ross v. Bernhard* was retroactive. In *Chevron* this Court stated:

> "In our cases dealing with the nonretroactivity question, we have generally considered three separate factors. First, the decision to be applied nonretroactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied, see, *e.g., Hanover Shoe v. United Shoe Machinery Corp., supra,* at 496, or by deciding an issue of first impression whose resolution was not clearly foreshadowed, see, *e.g., Allen v. State Board of Elections, supra,* at 572. Second, it has been stressed that "we must . . . weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation.' *Linkletter v. Walker, supra,* at 629. Finally, we have weighed the inequity imposed by retroactive application, for

> '[w]here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the "injustice or hardship" by a holding of nonretroactivity.' *Cipriano v. City of Houma, supra,* at 706." 404 U.S. at 106.

In the instant case, the Court of Appeals determined that *Ross* did not establish a new principle of law, but merely resolved a conflict in the circuits. See pp. 12a, Appendix hereto. This was based on the fact that *DePinto v. Provident Security Life Ins. Co.,* 323 F. 2d 826 (1963) required the legal issues in a derivitive suit to be tried to a jury. Underlying the Court of Appeals' statement is the idea that petitioners should have foreseen the outcome of the *Ross* case. This, however, cannot be the nature of the test the Court announced in *Chevron.* Surely, the fact that *Ross v. Bernhard* reversed a decision of the Second Circuit which had been relied on by the trial court is enough to meet the first test. This is shown from the opinion itself. In connection with the first test in *Chevron,* this Court cited *Hanover Shoe v. United Shoe Machinery Corp.,* 392 U.S. 481 (1968). In that case, the reliance test was not met because the Court did not find it necessary to overrule or reverse any prior decision or to announce any new rule of law. It is only in cases like *Hanover Shoe* that the first test would not be met.

To interpret the reliance test as requiring a consideration of the relative merits of the conflicting decisions or of the authoritative weight to be attributed them is absurd. But even if petitioners were held to such a test it has been met.

The analysis of the Court of Appeals not only misconstrues the historical precedents concerning derivative suits, but misapplies this Court's decision in *Ross.*

Prior to *Ross*, it was recognized that historically the stockholder's derivative suit had been considered a single cause of action tried in equity, and therefore, there was no right to a jury trial. The sole exception to this rule was the Ninth Circuit's decision in *DePinto v. Provident Security Life Ins., Co. supra*, which up to the time of *Ross*, had been followed by no court. *Ross v. Bernhard*, 396 U.S. 531, 546 (1970), (Mr. Justice Stewart, dissenting.)

The majority opinion in *Ross* moreover, recognizes the historical fact, that, since the common law refused to permit stockholders to sue derivatively on behalf of the corporation, equity provided the remedy. This remedy "was the derivative suit, viewed in this country as a suit to enforce a *corporate* cause of action against officers, directors and third parties." *Ross v. Bernhard*, 396 U.S. 531, 535 (1970).

Further, after discussing the cases involving treble damages, grounded in the anti-trust laws, the Court stated that where such penal damages were not involved, there was no authoritative federal case passing on the applicability of the Seventh Amendment to the trial of a legal claim in a derivative suit, but that this Court's opinions were "not inconsistent with the general understanding, reflected by the State court decisions and secondary sources, that equity could properly resolve corporate claims of any kind without a jury when properly pleaded in derivative suits complying with the equity rules." *Id.* at 537. This was the prevailing opinion, which continued after the Federal Rules were adopted in 1939, until *DePinto* in 1963. *DePinto*, was not followed by any court and the secondary sources still reflected the above stated "general understanding." James, *Right to a Jury Trial in*

Civil Actions, 72 YALE L.J.655 (1963); Note, *The Right to a Jury Trial in a Stockholders' Derivative Action*, 74 YALE L.J. 725 (1965). Until, *Ross*, this Court had not spoken, except in a manner consistent with the historical rule. Reliance by the lower courts upon the historical rule, established for well over 100 years, was thus based squarely upon precedent, history, and all commentators, who recognized that historically equity had exclusive jurisdiction over derivative suits, and that the shareholder's right to bring a corporate cause of action controlled the characterization of the entire action. It was thus generally agreed that there was no right to a jury trial in such suits. See Lattin, CORPORATIONS ch. 8, §3 (1959); 2 Hornstein, CORPORATION LAW AND PRACTICE, §730 (1959); 13 Fletcher, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS, § 5944 (1961 ed.); 5 Moore, FEDERAL PRACTICE, 38.38 [4] (2d ed. 1951).

Finally, in *Ross*, this Court for the first time applied the Seventh Amendment guarantee of a jury trial to stockholders derivation suits, which historically were not "Suits at common law", but equity actions. That this was a new constitutional standard is beyond question.

In the face of this prevailing opinion (except for the one exception–*DePinto*) and the discussion in *Ross* itself, the Court of Appeals, in its cursory discussion, misconstrued the law. *Ross* did, indeed, establish a new principle regarding jury trial in what had theretofore been traditionally an equity, non-jury matter.

The Court of Appeals clearly disregarded the thrust of the second test in *Chevron*. It ignored the prior history of the rule regarding the trial of stockholders' derivative actions, and it did not consider whether retrospective operation of the new rule would further or retard the rule of *Ross v. Bernhard.* The only statement by the Court apparently bearing upon this test is, "we fail to see how retroactive application will retard operation of the rule." See p. 13a, Appendix hereto. This rhetorical observation would have been equally applicable in any of the cases to which this Court has accorded prospective application. The Court of Appeals simply did not undertake the delicate balancing envisaged by this Court in laying down the second test in *Chevron.* It failed to determine the extent to which prospective application would promote, or retrospective application would retard, the effectuation of the purposes for the rule announced in *Ross v. Bernhard.*

Non-retroactive application did not retard the operation of the rule in *DeStefano* because the Court had not concluded that bench trials were unfair. In other words, *DeStefano* manifests no constitutional doubt that those convicted without jury trial were guilty of the acts charged, or were denied due process. Similarly, there can be no constitutional doubt that those plaintiffs who have had their day in court, in equity, have had their case fairly and completely judged. Furthermore, alternative methods were still available to those who could demonstrate that injustice had in fact resulted. If the Court of Appeals had found–which it did not–that the bench trial findings were clearly erroneous within the meaning of Rule 52(a) of the Federal Rules of Civil Procedure, it might have reversed the judgment in favor of the defendants in any case. It should not, however, have concluded that a weighing of the evidence was intended by the *Chevron* "merits-demerits" test. Its focus should have been on the nature of the constitutional right extended and whether its denial resulted in a serious flaw in the fact finding process.

Finally, with respect to possible inequity, the Court apparently applied this test by expressing its conclusion that enough evidence was introduced to submit one of the claims for relief to a jury. The Court said, "Our appraisal of the disclosures pertaining to the exchange of 140,000 shares of Vanadium Corporation stock for 222,107 shares of Susquehanna persuades us that it would not be inequitable to retry this case." See pp. 13a, Appendix hereto.

The Court of Appeals appears to have weighed, in applying the inequity test, the conflict between the circuits, the predictability of the outcome, and even the sufficiency of the evidence. Again, the Court of Appeals missed the true nature of the test. Inequity results in this case because after over five years of litigation including appeals and a five week trial, the defendants were exonerated and should not be compelled to defend the action in another trial unless on traditional grounds—and none exist—error occurred at the trial which requires a new trial.

The Court of Appeals, however, considered none of the "competing conceptual and jurisprudential theories" bearing on the problem of retroactivity. *Tehan v. Shott,* 382 U.S. 406, 409 (1966). Instead it gave summary treatment to the tremendously important and significant constitutional problem presented. This Court should consider the question.

This treatment by the Court of Appeals justifies the grant of certiorari to review the judgment below.

2. THE COURT OF APPEALS HAS MISCONSTRUED AND MISAPPLIED THE OPINION OF THIS COURT IN ROSS v. BERNHARD, AND HAS THEREBY EXTENDED THE SEVENTH AMENDMENT BEYOND THAT CASE.

In *Ross v. Bernhard,* the derivative suit involved claims against the directors of the corporation and a third party, the corporation's brokers. The directors were accused of converting corporate assets, gross abuse of trust, gross misconduct, willful misfeasance, bad faith and gross negligence. *Ross v. Bernhard,* 396 U.S. 531 (1970). Both the directors and the broker were accused of breaches of fiduciary duty, and the broker was accused of breach of contract. In the instant case, claims under the Securities Acts were made against directors of the corporation.

In discussing the "legal claims" which it held should be tried to a jury, the Court of Appeals described them as two claims for damages, involving (1) the exchange of shares of Vanadium Corporation of America stock for its won shares, and (2) the issuance of new shares to former American Gypsum shareholders in the merger. The Court stated that, of the Securities Acts involved, §10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b)) and Rule 10b-5 thereunder (17 C.F.R. §240, 10b-5) had most direct relevance to these claims. The Court of Appeals characterized these claims as based upon fraud and deception. See pp. 18a, 23a, Appendix hereto. The third claim was based upon an alleged deficiency in the merger proxy statement; *i.e.,* if plaintiffs' version of the sale of Vanadium were accepted, the proxy description of that transaction was misleading. The claim based upon the proxy material, therefore, is based entirely upon the claim of fraud and breach of fiduciary duty by the directors. If there is no fraud, there is no issue as to the proxy material. The other claims were found to be equitable in character. See pp. 29a, Appendix hereto.

We have here claims against corporate directors for fraud and for breach of fiduciary duty. This is the historic situation which caused equity to provide a method of calling corporate managers to account. *Ross v. Bernhard,* 396 U.S. 531, 534 (1970). In this country, at least as early as *Robinson v. Smith,* 3 Paige Ch. R. 222 (N.Y. 1832) this principle was enunciated.

The fraud claims, the breach of fiduciary duty, would never have been tried to a jury, historically. Even in *DePinto v. Provident Securities Ins. Co.,* 323 F.2d 826 (9th Cir. 1963), the Ninth Circuit seemed to recognize this fact in determining the question of jury trial, concluding that a finding of breach of fiduciary duty rested upon a finding of gross negligence, and that when such a breach rests on negligence, the question was for a jury.

This Court, in *Ross,* recognized this factor. There, the Court stated:

> "There are allegations in the complaint of a breach of fiduciary duty, but there are also allegations of ordinary breach of contract, and gross negligence. The corporation, had it sued on its own behalf, *would have been entitled to a jury's determination,* at a minimum, *of its damages against its broker under the brokerage contract and of its rights against its own directors because of their negligence.* Under these circumstances *it is unnecessary to decide whether the corporation's other claims are also properly triable to a jury.*" *Ross v. Bernhard,* 396 U.S. 531, 542 (1970). (Emphasis added).

Whereas, in *Ross*, this Court did not decide whether such claims were properly triable to a jury, the Court of Appeals made the leap and did so determine. The Court of Appeals, in effect, has extended the Seventh Amendment to apply to actions beyond that which this Court chose to go in *Ross v. Bernhard.*

This result justifies the grant of certiorari to review the judgment below.

Finally, we may find the actual reason for the Court of Appeals' action in its statement that "Moreover, our appraisal of the disclosures pertaining to the exchange of 140,000 shares of Vanadium Corporation stock for 222,107 shares of Susquehanna persuades us that it would not be inequitable to retry this case." See pp. 13a, Appendix hereto.

The Court's opinion, especially its treatment of the evidence, shows that the Court of Appeals disagreed with the trial court's decision. However, to overturn that decision, the court would necessarily have to follow the "clearly erroneous" mandate of Rule 52(a), Fed. R. Civ. P. The evidence adduced in the case was such that the trial court's decision was clearly not erroneous. By misapplying, misconstruing and extending *Ross v. Bernhard,* however, the case was remanded for retrial, with a jury.

Additionally, in determining whether the evidence which plaintiffs adduced at the trial was sufficient to prove a *prima facie* case, to go to the jury, the Court not only ignored the salient fact that defendants rested their case after plaintiffs' case, but indulged in pure speculation as to what a jury might infer. "[T]he essential requirement is that mere speculation be not allowed to do duty for probative facts." *Galloway v. United States,* 319 U.S. 372, 395 (1943). To allow such a finding would let "speculation run riot. Speculation cannot supply the place of proof." *Moore v. Chesapeake & Ohio Ry. Co.*, 340 U.S. 573, 578 (1951). The Court of Appeals, however, in determining whether or not the evidence was such that a *prima facie* case had been made, indulged in just such speculation as it, upon reviewing a jury verdict containing such speculation against the evidence, would have been obliged to strike down. The action of the Court of Appeals for the Seventh Circuit in these instances cannot be justified.

3. THIS COURT HAS FREQUENTLY GRANTED CERTIORARI TO SETTLE QUESTIONS CONCERNING THE RETROACTIVITY OF ITS DECISIONS.

Ross v. Bernhard, supra was a decision which will have far reaching effects. This Court has frequently granted certiorari to settle questions concerning the retroactivity of its decisions. This case presents the question with respect to *Ross v. Bernhard*. Moreover, the Court of Appeals' opinion departs so far from the principles stated in *Linkletter, DeStefano,* and *Chevron* itself, that its opinion should be reviewed.

CONCLUSION

For these reasons a writ of certiorari should issue to review the judgment and opinion of the Seventh Circuit.

Respectfully submitted,
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May 25, 1972

APPENDIX A

In the
United States Court of Appeals
For the Seventh Circuit

SEPTEMBER TERM, 1971 SEPTEMBER SESSION, 1971

No. 18572

WILLIAM DASHO, DASHO-ROGERS, INC. and MAURICE H. SCHY,
Plaintiffs-Appellants,
vs.
THE SUSQUEHANNA CORPORATION, RALPH A. L. BOGAN, JR., EDWARD O. BOSHELL, M. M. HARDIN, HERBERT F. KORHOLZ, J. PATRICK LANNAN, HOWARD J. LAUHOFF, A. D. MARTIN, J. EARLE MAY, HUGH C. MICHELS, AKSEL NIELSEN, D. W. REEVES, R. C. SCHENK, FRANKLIN B. SCHMICK, HAROLD C. STUART, ALBERT W. THOMSON, FRANCIS C. WOOLARD and AMERICAN GYPSUM CO.,
Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 65 C 1757

Hon. ABRAHAM L. MAROVITZ, *Judge.*

JANUARY 18, 1972

Before FAIRCHILD, CUMMINGS and STEVENS, *Circuit Judges.*

STEVENS, *Circuit Judge.* American Gypsum Company was merged into Susquehanna Corporation on December 13, 1965. Plaintiffs, as shareholders of Susquehanna, commenced this action in advance of the merger for the purpose of preventing its consummation and also to recover damages for Susquehanna and its pre-merger shareholders. The district court refused to enjoin the merger and dismissed Count I of the complaint which asserted claims under § 17(a) of the Securities Act of 1933 [1] and § 10(b) of the Securities Exchange Act of 1934. [2] Proceedings under Count II, which asserted that the pre-merger proxy solicitation violated § 14(a) of the 1934 Act, [3] were apparently stayed pending the appeal to this court from the dismissal of Count I.

Count I alleged that Susquehanna had been harmed not only by the merger but also by an earlier purchase of 222,107 of its own shares at an excessive price. We held that the allegations of fraud or deception in connection with each of these securities transactions were sufficient to state a federal claim under § 17(a) and § 10(b). *Dasho* v. *Susquehanna Corporation,* 380 F.2d 262 (7th Cir. 1967), *cert. denied,* 389 U.S. 977.

Following the remand, there were protracted proceedings in the district court. Count II of the complaint was reinstated, defendants answered, portions of their answers were stricken, extensive discovery was conducted, plaintiffs' request for a jury trial was denied, they amended their complaint, plaintiffs voluntarily dismissed three defendants, the court held a lengthy trial, and thereafter plaintiffs filed still another amended complaint to conform their final theories of the case to the proof. In that pleading they abandoned all charges of conspiracy.

The district court entered extensive findings of fact, conclusions of law, and judgment for the defendants on all claims. On this appeal plaintiffs contend that it was error to strike their jury demand, that the district court misconceived their theory of the case, that critical findings are clearly erroneous, and that vital evidence was improperly excluded. The threshold question is whether *Ross* v. *Bernhard,* 396 U.S. 531, which was decided by the Supreme Court after the trial was concluded, requires us to hold that it was error to deny plaintiffs a jury trial. Since we have concluded that it does, we must also identify the issues which should be submitted to a jury for determination when the case is remanded for a new trial.

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[1] 15 U.S.C. § 77q.

[2] 15 U.S.C. § 78j.

[3] 15 U.S.C. § 78n.

Before discussing the legal issues, we shall identify the defendants and describe the three securities transactions which gave rise to plaintiffs' derivative action.

I.

Susquehanna is a large publicly owned corporation. In April and May of 1965 its shares were traded over the counter in the range between a low bid of 11-½ and a high asked price of 14-⅛. At the time of its annual meeting on April 19, 1965, approximately 2,760,000 shares were outstanding, owned by some 8,750 stockholders. At that meeting 15 directors were elected, 13 proposed by management and 2 by a group in Kansas City who had cumulated their votes to oppose the management slate. The 13 management directors, led by J. Patrick Lannan, the chairman of the board, owned or controlled about 436,000 shares; however, substantial additional amounts of Susquehanna stock were owned by friends or associates of the 13 management directors and by the Kansas City group represented by the two dissidents.

Prior to May 25, 1965, neither American Gypsum Company, over half of whose shares were controlled by defendant Herbert F. Korholz, nor Korholz himself, owned any Susquehanna stock. After consummation of the three transactions which plaintiffs challenge, Korholz had become Susquehanna's principal shareholder, and the management directors, as well as the Kansas City group, had sold a major portion of their holdings.

On May 25, 1965, Korholz purchased 430,000 shares from Lannan, certain management directors, and their friends and relatives at a price of $15 per share. On August 11, 1965, in a transaction negotiated by Korholz, Susquehanna purchased 222,107 of its own shares from the Kansas City group at a price of either $13.85 or $10.78 per share, depending on whether plaintiffs' or defendants' version of the transaction is accepted. On December 13, 1965, to consummate the merger with Gypsum, Susquehanna issued 1,274,734 shares to the former shareholders of Gypsum, including Korholz, in an exchange which was based on a determination that Susquehanna's stock had a fair value of $10.75 per share. One of the assets acquired by Susquehanna via the merger was the block of 430,000 of its own shares which Korholz had purchased from Lannan and thereafter conveyed to Gypsum; one of the liabilities was the bank indebtedness of $6,450,000 which Gypsum had incurred to finance the 430,000 share purchase.

The defendants may be identified in four groups: The Lannan defendants who sold out and resigned from the board in May or shortly thereafter;[4] the eight members of Lannan's board who remained as directors and shareholders after he sold out;[5] the two dissidents representing the Kansas City group;[6] and Korholz and his associates.[7] Since plaintiffs' conspiracy charge has been abandoned, the different defendants obviously do not share equal responsibility for each of the three transactions which took place on May 25, August 11, and December 13, 1965. Although these transactions were not unrelated, we shall describe them separately.

1. The purchase of 430,000 shares by Korholz on May 25, 1965, was the consequence of discussions between Korholz and representatives of Lannan earlier that month. The price of $15 per share was about $3.00 over the market when it was agreed upon, subject to certain conditions. Korholz's offer was conditioned upon the resignation of five members of the Susquehanna board, including Lannan,

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[4] Lannan, Lauhoff and Wirtz resigned from the board on May 18, 1965, and sold all of their Susquehanna stock a week later. Schmick and Bard also sold all of their stock but did not resign until June 18 and July 15, respectively. Wirtz and Bard were voluntarily dismissed by plaintiffs on the first day of trial; Lannan, Lauhoff and Schmick contend that they have no responsibility for what happened after their resignations from the board.

[5] Schenk, Bogan, Boshell, May, Michels, Stuart, Mason and Woolard were members of Lannan's management slate and remained on the board, and continued to own Susquehanna stock until after the merger. Mason owned only 100 shares; he was the third defendant voluntarily dismissed by plaintiffs.

[6] Martin and Thomson were the two directors elected by a group of shareholders who were apparently customers of a broker in Kansas City named Coen. They had no advance knowledge or participation in the original sale of 430,000 shares to Korholz, but were familiar with the transaction with Coen in August and the merger in December.

[7] Korholz is the principal defendant. Hardin, Nielsen and Reeves were his nominees to replace the members of the Lannan management who resigned on May 18, 1965, or shortly thereafter. Gypsum, the corporation of which Mr. and Mrs. Korholz owned or controlled 37% before its merger into Susquehanna, is also a defendant.

the election of Korholz as chairman of the board of directors and as a member of the Executive Committee, and the election of two Korholz nominees (Nielsen and Hardin) to the Susquehanna board.

The offer was communicated to all 13 management directors, but not to the two dissidents or to the public. The five directors who were to resign sold their Susquehanna stock; the remaining directors made significant contributions to the 430,000 share package, either from their own holdings or from stock owned by friends and relatives,[8] but each retained an investment in Susquehanna.[9] Before they voted to elect Korholz, Nielsen, and Hardin to the Susquehanna board, the remaining directors had been advised about the business experience and integrity of the new directors and presumably also knew that the sale of the 430,000 shares at the $15 price was contingent upon their election.

The district court found, however, that the old directors were not aware of the fact that Korholz was making the purchase on behalf of Gypsum rather than as an individual investment. He made the offer and closed the transaction in his individual capacity because Gypsum was disabled from obtaining the necessary financing without the consent of two insurance companies to which it owed several million dollars. Korholz had received informal assurance that such consents would be forthcoming and, therefore, had been able to borrow $6,450,000 from The First National Bank of Boston on the understanding that Gypsum would assume that indebtedness and acquire the 430,000 shares of Susquehanna as soon as conditions specified by the insurance companies had been met. Those conditions included the election of Korholz as chairman and two of his designees as members of Susquehanna's board of directors, and an assurance from Gypsum that if it were merged into Susquehanna, the merged company would promptly repay the bank loan of $6,450,000.

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[8] Thus, for example, Bogan, who owned or controlled 56,152 shares at the time of the annual meeting in April, delivered about 65,000 shares into the package and still retained 13,986 shares on September 15, 1965, ding to the proxy statement. Woolard, who retained his own holding 800 shares, sold approximately 70,000 shares for his associates.

en of the remaining directors owned a significant number of shares after the Korholz purchase, ranging, at the time the proxy statement for the merger was prepared, from 64,229 for Michels and 47,280 for May, to 2,147 for Schenk, the company president.

It is apparent that Korholz, Gypsum, and The First National Bank of Boston were conscious of the fact that Susquehanna's current assets exceeded its total liabilities by over $13,000,000 when the funds to finance the 430,000 share purchase were advanced. The management directors of Susquehanna apparently knew little more than that Korholz, a capable and imaginative executive, was prepared to pay a premium price of $15 per share for about 15% of Susquehanna's stock and to accept a position of major responsibility in the direction of the corporation's affairs.

Precisely what public announcement of the transaction was made is not clear from the record. The district court found that "when the information as to facts was publicly released promptly after the May 18 board meeting, there was no effect whatsoever on the price of Susquehanna in the over-the-counter market."

The first transaction resulted in a significant change in the ownership of Susquehanna's stock and in the composition of its management, but it had no direct impact on the corporation's assets, liabilities, or capital structure. The balance sheet of Gypsum, however, was materially affected as soon as the arrangements to finance the purchase price had been concluded. It acquired a $6,450,000 asset, consisting of the block of 430,000 shares of Susquehanna, and a new liability of an equivalent amount, represented by the bank loan. Gypsum retained this asset and this liability until it was merged into Susquehanna in December.

2. In the second transaction which was closed on August 11, 1965, Susquehanna acquired 222,107 of its own shares and $300,685 in cash in exchange for 140,000 shares of the stock of Vanadium Corporation of America which Susquehanna had owned for four or five years. The transaction was closed through an escrow at The First National Bank of Boston in which three parties, Susquehanna, M. Coen, representing the Kansas City group, and Vanadium, all made deposits and withdrawals.

Vanadium deposited $3,377,500 in cash and withdrew 140,000 of its own shares;[10] Coen, on behalf of the Kansas

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[10] It promptly sent a letter to its shareholders reporting that it had made a favorable purchase of these shares at a price of $24.125 per share, a price which, though over the current market, was less than book value.

City group, deposited 222,107 shares of Susquehanna stock and made a net cash withdrawal of $3,076,815; Susquehanna deposited the 140,000 shares of Vanadium and withdrew the 222,107 shares of Susquehanna deposited by the Kansas City group and the cash balance of $300,685.

Three versions of this transaction have been put forward by the parties, one by the plaintiffs and two by the defendants.

Plaintiffs contend that Vanadium's payment of $3,377,500 established the value of the block of 140,000 of its shares, and that a simple calculation of the Susquehanna and Coen deposits and withdrawals reveals a purchase by Susquehanna of a block of its own shares for a price of $13.85, or a premium of about $3 over the market.[11]

Defendants contend that Susquehanna simply exchanged its block of Vanadium stock for 222,107 Susquehanna shares owned by the Kansas City group, and that the resale of the Vanadium stock for cash was a separate transaction to which Susquehanna was not a party. On the day before the exchange agreement was executed, the mean price for Susquehanna in the over-the-counter market was almost $11, and Vanadium closed at $19.25; the exchange agreement was predicated on a trade of 140,000 shares of Vanadium at $19.25 each (a total package of $2,695,000) for 250,000 shares of Susquehanna at $10.78 each, with a pro rata cash adjustment to be made if a lesser quantity of Susquehanna shares should be delivered.[12] Thus, under defendants' first version of the transaction, it was simply an exchange of shares on a market-to-market basis, without any premium attached to either block. In essence, this is the version of the transaction which was reported to Susquehanna's shareholders in the pre-merger proxy statement. Consistently with this interpretation, no disclosure was made of the resale of the Vanadium shares at a price of $24.125, which netted the Kansas City group a premium of $682,500. Defendants contended that such a premium could not have been realized in any sale by Susquehanna because an outstanding injunction prohibited Susquehanna from voting those shares.[13]

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[11] The net amount received by the Kansas City group ($3,076,815) divided by the number of Susquehanna shares delivered (222,107) equals a price of $13.85.

[12] Thus, the difference between the maximum purchase of 250,000 shares and the 222,107 shares actually delivered accounts for the cash distribution to Susquehanna of $300,685.

Plaintiffs offered evidence to prove that defendants knew, or should have known, that a premium was obtainable for the block of 140,000 shares of Vanadium, and that the premium value had been deliberately made available to the Kansas City group to forestall threatened litigation and possible opposition to a merger with Gypsum.[14]

Defendants' second version of the transaction was that the directors, acting in good faith and exercising an informed, independent business judgment, might deliberately make a premium available to the Kansas City group in order to eliminate the divisive influence on the board represented by the two dissident directors, thereby permitting Susquehanna to function more effectively and harmoniously. The two dissidents remained on the board and thereafter voted consistently with their colleagues. In substance, defendants' second interpretation of the August transaction is that if Susquehanna did, indeed, pay a premium price for the 222,107 shares purchased from the Kansas City group, a corporate benefit of equivalent value was received, or at least the directors in good faith so believed. Under this version it is not entirely clear to us whether defendants are contending that the "informed business judgment" of the directors included knowledge that a premium was being made available to the Kansas City group.

The district court entered findings proposed by defendants which appear to accept both of defendants' versions of this transaction.

3. In the merger consummated on December 13, 1965, Susquehanna in effect "sold" 1,274,734 newly issued shares

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[13] See *Vanadium Corp. of America v. Susquehanna Corp.*, 203 F.Supp. 686, 697 (D.Del. 1962).

[14] Coen, representing the Kansas City group, addressed a letter to the Susquehanna directors threatening to commence litigation to recover the premium portion of the price received by Lannan and the other selling parties in May and to enjoin Korholz and his associates from acting as directors and from voting any of the shares purchased from Lannan. Korholz thereafter proposed the exchange of Vanadium stock for the stock represented by Coen. After the exchange was authorized by the Susquehanna board on July 15, 1965, Korholz introduced Coen to the Vanadium principals with whom he negotiated the resale. He formally withdrew his threat of litigation by letter of August 10.

to the Gypsum shareholders in exchange for the assets and liabilities of Gypsum. One new share of Susquehanna was issued in exchange for each 1.9 shares of Gypsum. This exchange ratio was determined by New York Hanseatic Corporation and reviewed by Stone and Webster, both being recognized as experts in such matters, and both expressing the opinion that an exchange ratio of 1.9 to 1 was fair to both groups of shareholders.

In calculating the exchange ratio, the experts ignored Susquehanna's earnings, having determined that its "break up" value exceeded its worth as a going concern. They concluded that the total market value of its net assets[15] was approximately $27,135,000. which was equal to $10.75 for each share outstanding. Thus, in effect, the price of the Susquehanna shares "sold" via the merger was $10.75.

In calculating the value of Gypsum's contribution to the merged enterprise, the experts capitalized its earnings. As reported in the proxy statement, Gypsum's earnings for the years 1961 through 1965 had been 4, 5, 41, 45 and 33 cents per share respectively. The experts' calculation was not, however, based on the reported earnings. They determined that the elimination of nonrecurring losses and the addition of projected profits warranted an upward adjustment in the earnings for the year ended June 30, 1965, to 56-½ cents per share. They then applied a capitalization rate of 10% and concluded that the Gypsum shares were worth $5.65 each.[16] The relationship between $5.65 per share of Gypsum and $10.75 per share of Susquehanna produced the 1.9 to 1 exchange ratio.

In their report the experts also prepared a schedule showing the relationship between the market prices of Susquehanna and Gypsum for each month between January, 1964, and July, 1965. During most of those months a ratio based on comparative market values would have been more favorable to Gypsum,[17] but in the first four months of 1965 it would have been somewhat more favorable to Susquehanna, ranging between 1.92 to 1 and 2.02 to 1 during those months.

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[15] They treated a federal income tax loss carryover as an "asset" with a value of about $2,900,000. The gross amount of the carryover was reported in the proxy statement at $14,400,000 as of December 31, 1964.

[16] Gypsum's "adjusted earnings for the 12 months ended June 30, 1965" as determined by the experts were $1,374,000. (PX 72, p.8) Applying the capitalization rate of 10%, they thus assumed that the value of Gypsum's contribution to the merged enterprise was aproximately $13,740,000 as compared with their appraisal of Susquehanna's "break up" value at approximately $27,135,000.

The experts took note of the fact that one of Gypsum's major assets was its ownership of 430,000 shares of Susquehanna stock. Those shares were carried on Gypsum's books at their cost of $6,450,000 (or $15 per share). With its investment in Susquehanna valued at cost, Gypsum's stock had a book value of $2.20 per share, as reported in the proxy statement. Since, however, the experts had appraised Susquehanna stock as worth only $10.75 per share (as compared with the $15 cost on Gypsum's books), they recognized that the value of Gypsum's ownership of 430,000 Susquehanna shares should be reduced by $1,827,500 (430,000 times $4.25 per share), and that such an adjustment would reduce the Gypsum stockholders' equity to about $3,984,000,[18] or approximately $1.53 per share. This adjustment, as well as Gypsum's heavy indebtedness, was a factor considered by New York Hanseatic in determining the 10% capitalization rate for Gypsum. It noted that Gypsum stock had been valued in the market "historically" at 13 to 18 times earnings, and, therefore, the multiple of 10 was considered appropriate.[19]

The two companies distributed a joint proxy statement, as well as a series of supplementary letters, in which they reported that the directors of both companies unanimously favored the merger. In essence, Susquehanna was contributing a strong balance sheet and a large tax loss, and Gypsum was contributing earnings potential, to a mutually beneficial combination. The proxy statement reported the conclusions of New York Hanseatic and Stone and Webster, but omitted any explanation of the basis of the experts' evaluations.

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[17] Thus, for example, in January of 1964 the ratio would have been 1.15 to 1, and in July of 1965, 1.62 to 1.

[18] The experts' opinion does not give complete details on how this figure was arrived at, but we accept it as accurate enough for our purposes.

[19] They made no comment on the fact that the conservative multiple of 10 times the adjusted earnings of 56-½ cents produced a higher value than a liberal multiple of 17 times the audited earnings of 33 cents per share.

Plaintiffs contend that the proxy statement omitted, or inaccurately stated, a number of material facts. They criticized the descriptions of the original Korholz purchase, of the purchase from the Kansas City group, and of the extent of Korholz's control over the management of the company and the planning of the merger.

The merger was approved by the shareholders of both companies; 97% of the shares of Gypsum were voted affirmatively in favor of the merger and 75% of the shares of Susquehanna. Thus, over 200,000 votes more than the required 66-2/3% of the Susquehanna votes needed for approval were obtained. Approximately 25% of the shares either did not vote or voted against the merger.

II.

Defendants contend that plaintiffs were not entitled to a jury trial because (a) *Ross* v. *Bernhard,* 396 U.S. 531, which was decided on February 2, 1970, announced a new rule of constitutional law that is inapplicable to the trial in this case which was concluded on October 22, 1969; (b) plaintiffs' jury demand was not timely; and (c) in any event it related to only three of the 18 defendants. We have concluded that none of these arguments is supportable.

A.

To support their contention that *Ross* v. *Bernhard* does not apply retroactively, defendants rely on *DeStefano* v. *Woods,* 392 U.S. 631. In that case the Supreme Court held that the decisions in *Duncan* v. *Louisiana,* 391 U.S. 145, and *Bloom* v. *Illinois,* 391 U.S. 194, would not be applied retroactively. In *Duncan* and *Bloom*, the Court had upheld a defendant's right to a jury trial in serious criminal cases, including criminal contempts. The argument here is that if the constitutional right to a jury trial is not enforced retroactively in cases involving personal liberty, *a fortiori,* there should be no retroactivity in litigation involving mere property rights.

The argument implies that nonretroactivity should have broader application in civil than in criminal litigation. In fact, however, "the nonretroactive application of judicial decisions has been most conspicuously considered in the area of criminal process." *Chevron Oil Co.* v. *Huson*, 40 U.S.L.W. 4023, 4026 (Dec. 6, 1971). There is almost no suggestion in any of the cases from *Linkletter* v. *Walker*, 381 U.S. 618, through *Mackey* v. *United States*, 401 U.S. 667 (see especially Mr. Justice Harlan's concurring opinion, 675-702) that this line of authority should be applied to civil litigation. Nevertheless, there are instances in which the "doctrine of nonretroactivity" has been applied in civil litigation. *Chevron Oil Co.* v. *Huson*, *supra*, at 4026.

In dealing with the nonretroactivity question, the Supreme Court has generally considered three separate factors. The first, which we consider decisive here, is whether the rule sought to be applied establishes "a new principle of law either by overruling clear past precedents on which litigants may have relied . . . or by deciding an issue of first impression whose resolution was not clearly foreshadowed." 40 U.S.L.W. 4026. In this case defendants' argument assumes that *Ross* v. *Bernhard* announced a new rule of procedure because there was no preexisting right to a jury trial in derivative litigation. This position was persuasively advanced by the majority of the Second Circuit in the opinion on which the court below relied,[20] and by Mr. Justice Stewart in his dissent in *Ross*, 396 U.S. 531, 543-551. We think it plain, however, that we must follow the rationale of the Supreme Court's majority opinion which merely held, in agreement with a 1963 decision of the Ninth Circuit,[21] that "the Seventh Amendment preserves to the parties in a stockholder's suit the same right to a jury trial that historically belonged to the corporation and to those against whom the corporation pressed its legal claims." 396 U.S. at 542. Under the analysis made in the Supreme Court's majority opinion, *Ross* did not establish a new principle of law. It merely resolved a conflict in the circuits consistently with the Court's interpretation of prior law.

The second factor in deciding the retroactivity question is whether, weighing the merits and demerits in each case, retrospective application will further or retard operation of the rule. The third requirement is that we weigh the possible inequities of retroactive application. Since there were conflicting rules in the circuits, the defendants knew that the issue was not settled and that the district court might be reversed on appeal. They were certainly aware of the Ninth Circuit's decision in the *DePinto* case, as well as the fact that a member of the Second Circuit panel in *Ross* v. *Bernhard* had filed a dissenting opinion. It is, therefore, no more inequitable here than in any other case presenting an unsettled question of law to require defendants, who could have avoided the issue by consenting to a jury trial, to bear the risk of reversal on appeal. Moreover, our appraisal of the disclosures pertaining to the exchange of 140,000 shares of Vanadium Corporation stock for 222,107 shares of Susquehanna persuades us that it would not be inequitable to retry this case. Finally, we fail to see how retroactive application will retard operation of the rule. Thus, though we consider the first criterion decisive, we have also considered and rejected any claim of nonretroactivity based on the second and third criteria.

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[20] *Ross* v. *Bernhard*, 403 F.2d 909 (2nd Cir. 1968), but see Smith, C.J., dissenting at p. 915.

[21] *DePinto* v. *Provident Security Life Ins. Co.*, 323 F.2d 826, *cert. denied*, 376 U.S. 950.

The basic reason for holding that a new rule will not be applied retroactively is to avoid unfairness to parties who may have acted in reliance on the old rule.[22] In this case, however, defendants do not seek to justify any aspect of their conduct of the three transactions challenged by plaintiffs by claiming reliance on a rule which antedated the Supreme Court decision in *Ross* v. *Bernhard*. Nothing more than trial tactics was involved in their motion to strike the plaintiffs' jury demand. This is not one of the exceptional situations in which a holding of nonretroactivity is required to avoid consequences akin to the enactment of an ex post facto law.

We hold that plaintiffs were entitled to demand a jury trial of any legal claims historically triable to a jury which they have asserted against defendants on behalf of Susquehanna Corporation.

B.

Defendants contend that plaintiffs' jury demand was not timely. It was filed more than 38 months after the original complaint and several months after all defendants had answered. It was incorporated in a reply which itself was not filed within the time specified by the court.

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[22] See Schaefer, The Control of "Sunbursts": Techniques of Prospective Overruling, 42 N.Y.U.L.R. 631 (1967); Fairchild, Limitation of New Judge Made Law to Prospective Effect Only: "Prospective Overruling" or Sunbursting, 51 Marquette L.R. 254, 257 (1967-68).

Defendants rely on cases holding that after the right to a jury trial has been waived, the right cannot be revived by a belated amendment to the pleadings which does not raise any new issues.[23] However, a review of the proceedings in this case persuades us that there was no point in time when it could fairly be said that plaintiffs had waived their right to demand a jury.

Rule 38(b) permits a party to postpone decision on whether or not to demand a trial by jury until after the issues to be submitted to the jury have been finally framed by the pleadings.[24] Presumably, that is the reason the timeliness of a jury demand is measured from the filing of the "last pleading directed to such issue," and also why amendments which do not really change the issues do not revive a right that has been waived.

In this case plaintiffs cannot be charged with sole responsibility for the time which elapsed before the case was finally at issue. The sufficiency of Count I of the complaint was tested by motions to dismiss which led to the first appeal to this court. After the remand, defendants filed their answers in February and March of 1968. Plaintiffs promptly moved to strike several portions of the answers, including parts of all five affirmative defenses asserted by defendants Korholz, Gypsum and Susquehanna. Those motions raised substantial questions which were briefed at length and led to the entry of an order on October 21, 1968, in which the court struck portions of the affirmative defenses and granted plaintiffs leave to file a reply by December 1, 1968. The reply was not actually filed until December 30, 1968, but no objection to its filing was made at that time.

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[23] See *Moore* v. *United States*, 196 F.2d 906, 908 (5th Cir. 1952); *Connecticut General Life Ins. Co.* v. *Breslin*, 332 F.2d 928, 931 (5th Cir. 1964); *Leighton* v. *New York, Susquehanna & Western R.R.*, 36 F.R.D. 248, 249 (S.D.N.Y. 1964).

[24] Rule 38(b) provides:

"(b) Demand. Any party may demand a trial by jury of any issue triable of right by a jury by serving upon the other parties a demand therefor in writing at any time after the commencement of the action and not later than 10 days after the service of the last pleading directed to such issue. Such demand may be indorsed upon a pleading of the party."

If the reply had been filed on December 1, 1968, quite clearly it would have been the "last pleading" within the meaning of Rule 38(b). Up to that time there had been no final definition of the issues and no waiver of the right to a jury trial. By permitting the reply to be filed on December 30, 1968, the trial court effectively extended the time for filing the "last pleading," and thus the time in which to demand a jury.

When the district court sustained the motion to strike the jury demand, he placed no reliance on its late filing. Commendably he made it perfectly clear that his ruling was based on the Second Circuit decision in *Ross* v. *Bernhard,* and he indicated at the hearing on the motion that if the law permitted a jury trial in a derivative action, he would not have rejected the demand as untimely. We hold that plaintiffs did not waive their right to a jury trial.

C.

The pleading which included the jury demand was identified as a reply to the affirmative defenses of only three of the defendants. It is, therefore, contended that the demand should be construed as limited to the issues raised in the affirmative defenses of those three defendants.

Even as so construed, however, it is clear that basic issues in the litigation were encompassed by the reply and, therefore, by the jury demand incorporated therein. The affirmative defenses squarely raised the question whether Susquehanna had been damaged by any of the alleged misconduct of the defendants, the question whether the merger exchange ratio was fair, and other important issues.

The broad language of the jury demand plainly indicated that plaintiffs wanted a jury trial of all issues which could properly be submitted to a jury. Defendants other than Korholz, Gypsum and Susquehanna construed the demand as applicable to them because they also filed a motion to strike. The trial judge viewed the problem as whether any jury trial was appropriate in a derivative action, and does not appear to have considered the possibility of separating out certain issues for the jury. We have no doubt that if the trial judge had had the benefit of the later Supreme Court opinion in *Ross* v. *Bernhard,* he would not have construed the demand in the restrictive manner which defendants urge here. Assuming that the demand was timely, as we have held, we think a fair construction of its broad language would cover all issues that plaintiffs are entitled to have tried by a jury. We, therefore, must identify those issues.

III.

Although the holding in *Ross* v. *Bernhard* makes it plain that plaintiffs, who are suing derivatively on behalf of Susquehanna, have "the same right to a jury trial that historically belonged to the corporation," 396 U.S. at 542, in that case the Supreme Court was not required to define the scope of that right. The opinion recognizes the possibility that some breaches of fiduciary duty by corporate directors may not be triable to a jury;[23] the reference to history in the statement of the holding implies that claims which are traditionally regarded as equitable in character may properly be heard by the court.

It is important to state the claims asserted by plaintiffs as precisely as possible, not only because we must differentiate between legal and equitable claims, but also because the relevant law is still in an embryonic stage of development and the Supreme Court has admonished us not to stunt its growth with "glib generalizations and unthinking abstractions."[24] We shall, therefore, first consider the two claims which we held sufficient on the prior appeal and then turn our attention to the several other claims which are included in the complaint as finally amended.

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[23] "In the instant case we have no doubt that the corporation's claim is, at least in part, a legal one. The relief sought is money damages. There are allegations in the complaint of a breach of fiduciary duty, but there are also allegations of ordinary breach of contract and gross negligence. The corporation, had it sued on its own behalf, would have been entitled to a jury's determination, at a minimum, of its damages against its broker under the brokerage contract and of its rights against its own directors because of their negligence. Under these circumstances it is unnecessary to decide whether the corporation's other claims are also properly triable to a jury. *Dairy Queen, Inc.* v. *Wood*, 369 U.S. 469 (1962)." 396 U.S. at 542-543.

[24] "Although § 10(b) and Rule 10b-5 may well be the most litigated provisions in the federal securities laws, this is the first time this Court has found it necessary to interpret them. We enter this virgin territory cautiously. The questions presented are narrow ones. They arise in an area where glib generalizations and unthinking abstractions are major occupational hazards. Accordingly, in deciding this particular case, remembering what is not involved is as important as determining what is." *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 465.

For purposes of identification we shall refer to the two principal claims as Susquehanna's (a) "purchase" and (b) "sale" of its own shares. The "purchase" was the acquisition of 222,107 shares from the Kansas City group in exchange for the block of Vanadium stock, and the "sale" was the issuance of 1,274,734 new shares to the former Gypsum shareholders at the time of the merger.

Also for identification purposes, we may list the additional claims which merit discussion as (1) the claim that the Lannan defendants received a premium for selling control of Susquehanna to Korholz; (2) a claim that § 10(b) and Rule 10b-5 were violated by failure to disclose the contemplated transfer of control before it took place; (3) a claim that the Lannan directors did not adequately investigate the qualifications of Korholz to be an officer and director of Susquehanna before his election; (4) a claim that the court should appoint a disinterested arbiter to redetermine the merger exchange ratio; and (5) a claim that deficiencies in the premerger proxy statement require that the merger be set aside.

We turn to the two claims for damages.

A. *Susquehanna's "purchase" of its own stock.*

Federal jurisdiction was properly invoked in this case because the complaint alleged violations of three federal statutes.[27] Of these three, it is § 10(b) of the Securities Exchange Act of 1934, and more particularly Rule 10b-5, that has most direct relevance to the claim that Susquehanna was damaged by paying too much in connection with the purchase of its own shares from members of the Kansas City group in August of 1965. The Rule plainly affords protection to both sellers and prchasers.[28] A private party

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[27] See footnotes 1, 2 and 3, supra.

[28] *Supt. of Ins. v. Bankers Life & Cas. Co.*, 40 U.S.L.W. 4001, 4002 (Nov. 8, 1971); *Birnbaum v. Newport Steel Corp.*, 193 F.2d 461, 463 (2nd Cir. 1952). Rule 10b-5 provides:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

"(a) To employ any device, scheme, or artifice to defraud,

"(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the state-injured by a violation of the Rule may either rescind his purchase or sale or recover his damages in an action at law.[19] It seems clear that a jury trial is appropriate in such a damage action.[20]

In this case there is no doubt that Susquehanna's acquisition of its own shares in exchange for its block of Vanadium stock was a "purchase" within the meaning of the Rule. Plaintiffs contend that as a direct consequence of fraud or deceit proscribed by the Rule, the purchase was made at a price which was unfair to Susquehanna.[21]

The perpetrators of the alleged fraud included several of the directors of Susquehanna. Since the challenged transaction did not require shareholder approval, the directors would normally speak for the corporation in connection with the matter. To the extent that the directors were competent to act for the corporation, it therefore would follow that Susquehanna was the victim of its own fraud.

This theoretical dilemma has been met in other cases by recognizing that defendant directors may deceive disinterested members of the board, and through them the cor-

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[18] (Continued)

ments made, in the light of the circumstances under which they were made, not misleading, or

"(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security." 17 CFR § 240.10b-5 (1971).

[19] The Supreme Court has clearly indicated that its holding in *J. I. Case Co.* v. *Borak*, 377 U.S. 426, encompasses an action for damages. See *Bivens* v. *Six Unknown Federal Narcotics Agents*, 403 U.S. 388, 397. Note also the comment by Mr. Justice Harlan in his concurring opinion at p. 402:

> "Thus, in suits for damages based on violations of federal statutes lacking any express authorization of a damage remedy, this Court has authorized such relief where, in its view, damages are necessary to effectuate the congressional policy underpinning the substantive provisions of the statute. *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964); . . ."

[20] See, *e.g.*, *Myzel* v. *Fields*, 386 F.2d 718, 740-741 (8th Cir. 1967), cert. denied, 390 U.S. 951; *Esplin* v. *Hirschi*, 402 F.2d 94, 95 (10th Cir. 1968), cert. denied, 394 U.S. 928. See also *Dairy Queen, Inc.* v. *Wood*, 369 U.S. 469, 477-479.

[21] The price paid for the Susquehanna shares may, of course, properly be measured by the value of the consideration delivered to the seller by the purchaser. See *Mueller* v. *Korholz*, 449 F.2d 82, 86, 88 (7th Cir. 1971).

poration.[22] Plaintiffs relied on that theory in the presentation of their evidence and in their argument here. However, a different theory is embodied in the complaint.

The complaint alleges that the entire board was interested in the transaction and, therefore, was not competent to authorize the purchase by the corporation. Accordingly, it is contended that defendants were under a duty to make full disclosure of their adverse personal interests to the shareholders, and that the failure to make that disclosure, or to advise the shareholders that the exchange actually cost Susquehanna $682,500, constituted a fraud or deceit prohibited by Rule 10b-5. The sufficiency of that claim is established as the law of this case, see 380 F.2d 262 at 269-270, and we are satisfied that insofar as a damage recovery is sought, the allegations raise issues triable to a jury.

It does not necessarily follow that the case should be remanded for a new trial on those issues. For if the evidence which plaintiffs adduced at the trial before the court was not sufficient to prove a *prima facie* case, the denial of a jury trial was harmless error. We shall, therefore, consider whether the record contains evidence tending to prove that Susquehanna was deceived, that there was a causal connection between the deception and the purchase, and that it was damaged thereby.

Although the trial judge, after weighing the evidence, rejected the inferences which plaintiffs draw from the facts, we cannot say that either of defendants' versions of the transaction is so clearly correct that plaintiffs' proof failed as a matter of law. Defendants contend that the block of Vanadium stock had no greater value to Susquehanna than the current market because the shares could not be voted while owned by Susquehanna and that, in any event, the benefits received by Susquehanna from the settlement of the pending litigation with Vanadium and the elimination of potential dissension within Susquehanna's top management more than offset the premium value of the Vanadium stock (and thus the true over-the-market cost of the purchased Susquehanna shares). If either of these factual propositions is correct, the purchase did not injure Susquehanna and the damage action must fail. But there is certainly evidence in the record from which a jury could conclude that Susquehanna could have realized a premium—possibly the full $682,500[33]—on a sale of the Vanadium stock to a third party or to Vanadium itself, and further, that making peace with the Kansas City group did not necessarily produce a corporate benefit of comparable value. The evidence on the damage issue is, therefore, sufficient for submission to a jury.

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[22] *Ruckle v. Roto American Corp.*, 339 F.2d 24 (2nd Cir. 1964). See also *Supt. of Ins. v. Bankers Life & Cas. Co.*, 40 U.S.L.W. 4001, 4002-3 (Nov. 8, 1971).

There is also evidence tending to prove that material facts were not disclosed to Susquehanna (either to the shareholders or to all of the directors voting on the matter), and that the purchase might not have been consummated on the same terms if full disclosure had been made.

If plaintiffs' version of the transaction is correct, the purchase resulted in a net injury to Susquehanna of approximately $682,500. Neither this fact nor the fact that a threat of litigation was avoided by making the exchange was ever disclosed to the shareholders. Such nondisclosure would not violate Rule 10b-5, however, if a disinterested majority of the board of directors was fully informed about all relevant facts, and if in the good faith exercise of their business judgment they concluded that the transaction was in the best interests of the corporation.[34] For on that hypothesis, since a disinterested majority of the board would have the authority to consummate the transaction, the disclosures within the board would constitute disclosure to the corporation.

A violation of Rule 10b-5 did result, however, if either of two factual propositions is established by the evidence. First, if material facts were misrepresented or withheld from some members of the board of directors, the corporation was deceived. *Ruckle* v. *Roto American Corporation*, 339 F.2d 24 (2nd Cir. 1964). Second, if the entire board of directors was interested in the transaction, a duty of disclosure to the shareholders existed,[35] and the corporation was deceived by the nondisclosure. Although it is not entirely clear that the second proposition has enough evidentiary support to justify submission to a jury,[36] there is substantial evidence in the record tending to prove that there was inadequate disclosure, and possibly actual misrepresentation, of material facts within the board of directors.[37] The

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[33] The actual damages need not be the full $682,500. If Susquehanna itself could have sold only for a lesser premium, that lesser premium would be the measure of damages. Or, if the jury valued the benefits received as greater than the market value of the Susquehanna shares but less than the full value of the Vanadium shares sold, the difference would be the damage recoverable.

[34] *Kors* v. *Carey*, 158 A.2d 136, 139, 141 (Del. 1960); *Warshaw* v. *Calhoun*, 221 A.2d 487 (Del. 1966).

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[35] See 380 F.2d at 270.

[36] Most of the directors apparently owed no special allegiance to Korholz. There appear to be three aspects of the "interest" of such directors in the transaction involving Vanadium stock: (1) to remove possible opposition to the Gypsum merger; (2) to eliminate dissension within the board; and (3) to avoid Coen's threatened litigation. The first two aspects of their interest would not conflict with their status as shareholders or directors. The third aspect might, however, if the evidence indicated that the director was a potential defendant in the threatened litigation and that it was reasonable to infer that the threat was of sufficient importance to influence his action as a director. The marginal character of the exposure of certain directors, when compared with the substantial character of their interest as shareholders in the welfare of the corporation (Michels, for example, owned over 64,000 shares), makes it extremely doubtful that their independence was compromised by the threat contained in Coen's letter of June 17, 1965, which can be read as not contemplating any claim at all against some members of the board. However, since plaintiffs will have the right to offer additional evidence at the retrial, and since we may have overlooked evidence which the trial judge might consider significant, we do not squarely decide the issue. We believe it is probably in the area in which we would respect the trial judge's discretion, whichever way he ruled, because of his superior ability to evaluate the evidence as it is actually presented.

[37] For example, the minutes of the July 15, 1965, meeting of the Susquehanna board of directors contains the following:

> "It was further reported to the Board that efforts had been made by Susquehanna without success to sell its Vanadium shares for a price in excess of market. Those shares were recently offered by Mr. Korholz and Mr. William L. Brown of The First National Bank of Boston to International Mining Corporation, as well as to Vanadium on that basis, but both such corporations had rejected the offer.
>
> "Mr. Korholz then reported that with the consent of the Executive Committee he had discussed with Mr. M. J. Coen of Kansas City, a possible exchange of the Vanadium shares for 250,000 shares of Susquehanna said to be owned by Mr. Coen and customers or his associates. Such discussion had resolved itself into a possible exchange on the basis of market values since Mr. Coen refused to pay a substantial premium for the Vanadium shares unless a comparable premium was paid for his block of Susquehanna shares." PX 1-R, pp. 5-6.

If this were all that was disclosed, and if Korholz had been aware of the possibility of Vanadium Corporation itself buying the stock at a premium, the jury could certainly conclude that he withheld such information from other members of the board in order to arrange the premium for Coen and persuade Coen to withdraw threatened litigation. There was also testimony that Korholz had previously called Coen and evidence of fraud or deception was thus sufficient to raise an issue for the jury.

Finally, we are persuaded that if the jury should accept plaintiffs' appraisal of the true impact of the transaction on Susquehanna, and if it should conclude that some of the directors were misled by Korholz, it would also be entitled to find a causal connection between the fraud and the injury. We, therefore, hold that plaintiffs are entitled to have a jury decide the issues raised by their claim that the purchase of 222,107 of its shares from the Kansas City group in July of 1965 resulted in damage, possibly as much as $682,500, to Susquehanna.

B. *Susquehanna's "sale" of its own shares.*

From Susquehanna's point of view, the statutory merger involved a sale of 1,274,734 of its own shares, and a purchase of 2,421,996 shares of Gypsum. *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 467-468; *Dasho* v. *Susquehanna Corp.*, 380 F.2d 262, at 268-269, *cert. denied*, 389 U.S. 977; *Swanson* v. *American Consumer Industries, Inc.*, 415 F.2d 1326, 1330 (7th Cir. 1969). Since interstate facilities were employed to consummate the exchange, the merger was a "securities transaction" covered by Rule 10b-5.

If it was the product of fraud or deception proscribed by the Rule, and if Susquehanna thereby suffered a pecuniary injury, a cause of action for damages may be prosecuted by plaintiffs on behalf of the corporation. Under *Ross* v. *Bernhard,* we believe such a claim would be triable to a jury. Before analyzing other elements of the claim, it is appropriate to consider the damage issue; unless the

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[37] (Continued)

asked him "whether he wanted to make some money on his investment or whether he just wanted to raise hell." (Tr. 447) And further, "[F]irst of all, get rid of this letter [threatening litigation] and then I will do it, we can work quietly on some program that gets you what you want as long as it is within reason and gets me what I want for the company." (Tr. 451) Following the July 15 meeting, Korholz accompanied Coen to New York and introduced him to Harder, a Vanadium director and a vice president of International Mining Co. which held substantial Vanadium stock. The purpose of the introduction was to help Coen sell the 140,000 shares. (Tr. 524-525) This evidence may not prove wrongdoing on the part of Korholz, but, taken with other evidence, could provide a basis for a jury to conclude that Korholz had deceived other members of the board.

record contains evidence on which an award of damages could be based, a jury trial may be unnecessary and our review may be limited to determining whether the district court findings on the issue of liability are clearly erroneous.

We find nothing in the record to suggest that Susquehanna should not have been merged with a profitable corporation in order to take full advantage of its tax loss. Nor do we find any evidence indicating that Gypsum was not an appropriate component of such a merged enterprise, or that a more favorable opportunity was lost because of the Gypsum merger. Thus, neither the fact that the merger took place, nor the fact that it was Gypsum that was merged into Susquehanna, appears to have caused any injury to Susquehanna.

Nevertheless, it is possible that the terms of the merger may have damaged Susquehanna. Even if it was wise to sell its shares to obtain Gypsum's earnings, Susquehanna may have been fraudulently induced to accept an inadequate price per share and therefore to issue too many shares.

For purposes of analysis we may assume that Susquehanna sold its own shares for a price of $10.75 per share and purchased Gypsum shares for a price of $5.65 per share. If either the former price was too low, or the latter price was too high, and if no compensating adjustment in the other is appropriate, Susquehanna was damaged. In other words, if the exchange ratio was unfair to Susquehanna, it was injured by the merger.

The district court found that the exchange ratio was fair. All the directors so testified, and plaintiffs offered no expert testimony to the contrary. The finding is further supported by the opinions of New York Hanseatic Corporation and Stone and Webster. Even though the finding is not clearly erroneous, indeed even if we would enter the same finding ourselves, it does not follow that the record contains no evidence from which a jury might have come to a different conclusion.

If the jury could properly find that Susquehanna's approval of the terms of the merger was obtained by fraud, and that a full disclosure of all material facts would have required an adjustment of those terms in order to obtain the necessary authorization to consummate the transaction, the conclusion that the corporation was in fact damaged by the fraud would be supportable. Assuming the existence of a violation and consequent injury, the question would then be whether the record contains any evidentiary basis for a reasonable calculation of the amount of that pecuniary injury.

Of course, damages may not be the product of pure conjecture or speculation. See *Bigelow* v. *RKO Radio Pictures,* 327 U.S. 251, 264. A jury cannot be permitted to make a random selection of any exchange ratio that might appeal to it. But if we assume that all other elements of the claim, except the amount of damages, have been adequately established, the same standards that juries employ to determine comparable issues in other complex commercial litigation would permit recovery here if the evidence provides a reasonable basis for measuring the injury. On that assumption, we have concluded that the record does contain evidence from which a jury could select an acceptable measure of damages.

It is not inconceivable that arm's length bargaining between fully informed representatives of Gypsum and Susquehanna would have produced an exchange ratio predicated on comparative market values during the months immediately preceding Gypsum's $6,450,000 investment in Susquehanna.[38] For each of the four months prior to May of 1965 such an approach would have produced a more favorable ratio for Susquehanna than 1.9 to 1. Viewing the transaction broadly, if, for example, the ratio of 2.02 to 1 or 1.96 to 1 had been used instead of 1.9 to 1, it could not be said that the total price paid by Susquehanna to acquire Gypsum's assets and earnings was beyond a tolerable range of fairness.[39] For on a 2 to

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[38] Following that investment, the value of Gypsum, relative to the value of Susquehanna, improved. If there was any causal connection between the investment and that relative change, it would suggest that Susquehanna, rather than Gypsum, was undervalued. For this purpose we assume that May should be considered the month in which Gypsum made its investment since Korholz was acting in its behalf.

[39] Thus, if such a "fair" ratio, rather than the actual ratio, also "fair" in abstract terms, would have been the ratio chosen by arm's length bargaining of fully informed parties, then such other ratio might be relevant in the computation of damages.

1 basis, assuming with the experts that Susquehanna's shares were worth only $10.75 apiece, it would have paid an aggregate price of approximately $13,000,000[40] for earnings of $814,000, as audited (or $1,374,000, as adjusted) and net assets of $3,984,000.[41]

We by no means suggest that this is the proper measure of damages in this case. Nor do we imply that market values are a better determinant of exchange ratios than expert appraisals. We merely hold that they provide a permissible measure damages from which a jury may estimate the amount of pecuniary damages which a defrauded party has suffered. We, therefore, conclude that if the record contains evidence tending to prove the other elements of plaintiffs' cause of action predicated on the merger, the claim for damages may be submitted to a jury. We now consider those other elements.

Plaintiffs must, of course, prove a violation of law by the defendants and a causal connection between the violation and an injury to Susquehanna. Plaintiffs have argued that there were several deficiencies in the proxy solicitation which violated SEC Rule 14a-9, implementing § 14(a) of the 1934 Act, and that the causation issue is settled by *Mills* v. *Electric Auto-Lite,* 396 U.S. 375. We are convinced that at least one of their attacks on the proxy statement raises a triable issue of fact, but we are not sure that *Mills* disposes of the causation issue in an action for damages. We first consider the violation.

The relevant language of Rule 14a-9 is similar to that found in Rule 10b-5[42] and § 29(a). The proxy solicitation was unlawful if it contained "any statement which . . . is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading. . . ." If a jury should agree with plaintiffs' version of the transaction in August 1965 (when Susequehanna used its block of Vanadium stock to purchase 222,107 of its own shares), it could also properly conclude that the description of that transaction in the proxy statement was misleading.[43] If plaintiffs' analysis is correct, the proxy statement falsely advised the shareholders that a purchase by Susquehanna of approximately $3,000,000 worth of its own shares had been made on a "market to market" basis when in fact a premium of $682,500, amounting to about $3 per share, was paid. The magnitude of the transaction, the fact that it related directly to the value of Susquehanna shares (and therefore to the fairness of the bargain which was the subject of the proxy statement), and the character of the omission or misstatement, all satisfy the test of materiality as stated by the Second Circuit in *General Time Corporation* v. *Talley Industries, Inc.*[44] To the extent that intent is relevant, the evidence is adequate.[45] Plainly, then, there was sufficient evidence of a violation to be submitted to a jury.

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[40] If Gypsum's 2,421,996 shares had been acquired on a 2 for 1 basis, Susquehanna would have issued 1,210,998 shares. At the price of $10.75 per share, the aggregate issue would have been worth $13,018,228.50. At the same price, the number actually issued on the 1.9 to 1 basis (1,274,734) was worth approximately $685,000 more.

[41] The figure of stockholder's equity used in the New York Hanseatic report.

[42] Both Rule 10b-5 and Rule 14a-9 apply to proxy solicitations in connection with a purchase or sale of a security. See *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 468; *Swanson* v. *American Consumer Industries, Inc.*, 415 F.2d 1326, 1331 (7th Cir. 1969).

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[43] Indeed, even if it should accept defendants' second version of the transaction and determine that the directors' "informed business judgment" included knowledge that a substantial premium was being made available to the Kansas City group, the proxy statement would be misleading because that information was not disclosed to the shareholders.

[44] "The test, we suppose, is whether, taking a properly realistic view, there is a substantial likelihood that the misstatement or omission may have led a stockholder to grant a proxy to the solicitor or to withhold one from the other side, whereas in the absence of this he would have taken a contrary course." 403 F.2d 159 at 162 (1968), *cert. denied*, 393 U.S. 1026. Since plaintiffs circulated a letter to the Susquehanna shareholders urging them to vote against the merger, we believe the comparative approach suggested by the Second Circuit as appropriate for proxy contests is also appropriate here.

[45] The "scienter" required in common law fraud is not necessary.

> "[K]nowledge of the falsity or misleading character of a statement and a bad faith intent to mislead or misrepresent are not required to prove a violation of the statute upon which a civil remedy for damages will lie." *Kohler* v. *Kohler Co.*, 319 F.2d 634, 637 (7th Cir. 1963).

See also *S.E.C.* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 854-855 (2d Cir. 1968), *cert. denied*, 394 U.S. 976, in which the court indicates that "lack of diligence, constructive fraud, or unreasonable or negligent conduct" may meet the state of mind requirement. *Id.* at 855. These cases discussed the required mental state in a 10(b)-5 case. The same requirements apply in a 14(a) proxy statement case. See *Butler Aviation Intern'l, Inc.* v. *Comprehensive Designers, Inc.*, 307 F.Supp. 910, 914 (D.C.N.Y. 1969), *aff'd*, 425 F.2d 842 (2d Cir. 1970); *Gerstle* v. *Gamble-*

On the question of causation, there is no doubt that the proxy solicitation was an essential link in the accomplishment of the merger. Apart from the solicitation, there is no contention that defendants could have mustered the necessary two-thirds vote required for the approval of the merger. The following language in the *Mills* opinion may, therefore, determine the causation issue:

> "Where the misstatement or omission in a proxy statement has been shown to be 'material,' as it was found to be here, that determination itself indubitably embodies a conclusion that the defect was of such a character that it might have been considered important by a reasonable shareholder who was in the process of deciding how to vote. This requirement that the defect have a significant *propensity* to affect the voting process is found in the express terms of Rule 14a-9, and it adequately serves the purpose of ensuring that a cause of action cannot be established by proof of a defect so trivial, or so unrelated to the transaction for which approval is sought, that correction of the defect or imposition of liability would not further the interests protected by § 14(a).
>
> "There is no need to supplement this requirement, as did the Court of Appeals, with a requirement of proof of whether the defect actually had a decisive effect on the voting. Where there has been a finding of materiality, a shareholder has made a sufficient showing of causal relationship between the violation and the injury for which he seeks redress if, as here, he proves that the proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction." 396 U.S. at 384-385.

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[45] (Continued)

Skogmo, Inc., 298 F.Supp. 66, 97 (D.C.N.Y. 1969) (even less "scienter" than required in a Rule 10(b)-5 case is required in a §14(a) case).

We feel it unnecessary to discuss the evidence in this case on the requisite mental state except to say that the evidence appears sufficient to warrant a jury finding that the requisite mental state existed. We note, of course, that if plaintiffs prevail on the intracorporate deception theory, then there may be some defendants who did not have the requisite state of mind.

There are two reasons why quotation of that language out of its context does not necessarily eliminate the causation issue in this case. In *Mills* the plaintiffs were seeking equitable relief, not damages as plaintiffs do here. In *Mills,* apart from any question of the fairness of the exchange ratio, plaintiffs sought to vindicate their right to be shareholders of a separate company rather than a larger, combined enterprise[46]; here the merger itself was apparently unobjectionable[47] and a damage award must, in effect, depend on a revision of the exchange ratio. Thus, although the *Mills* holding would seem to require a finding of "legal injury" caused by the violation, in this case that injury may not include any pecuniary loss.[48]

In short, we think *Mills* takes us this far: If plaintiffs prevail on the issue of materiality, they have also established that approval of the 1.9 to 1 exchange ratio was unlawfully obtained. But that approval caused Susquehanna monetary injury only if (a) Susquehanna would have been better off with no merger at all; or (b) a more favorable exchange ratio would have been available if there had been full disclosure. The first alternative is not supported by any evidence which has been called to our attention; the second requires an evaluation of the transaction from Gypsum's point of view as well as Susquehanna's. For if it were plain from the record that Gypsum's shareholders would not in any event have approved a merger on terms which required surrender of more than 1.9 of their shares for each Susquehanna share, then approval of those terms, even if unlawfully obtained, did not harm Susquehanna.

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[46] See the portion of footnote 5 appearing on page 383 of 396 U.S.

[47] In the letter which plaintiffs mailed to the Susquehanna stockholders urging a vote against the merger, they stated, in part:

> "We take no position here as to whether a merger between Susquehanna and American Gypsum is desirable. We do, however, take the position that based upon the information presently available to stockholders, the terms proposed seem grossly unfair to Susquehanna. *We, therefore, urge that you do not approve the merger on its present terms.*" (Emphasis in original.) DX-68, p. 3.

[48] We identified two different kinds of legal injury in *Swanson, supra*:

> "Defendants next assert that no injury can be shown because any corporate opportunities or going concern value of which the Peoria shareholders might have been deprived is retained by them by virtue of their continuing equity position in ACI. The short answer is that if the allegations of the complaint are proved, the Peoria shareholders were entitled to a more favorable exchange ratio than they were granted and may have had their equity position unfairly diluted. Moreover, as recognized by the Supreme Court in SEC v. National Securities, Inc., 393 U.S. 453, 467, 89 S.Ct. 564, 21 L.Ed. 2d 668, the fraudulent substitution of shareholder status in one company for the same status in another may constitute a cognizable legal injury in and of itself." 415 F.2d at 1332.

Plaintiffs argue that Gypsum was under significant economic pressure to effect the merger because of its heavy indebtedness and its commitment to repay the $6,450,000 bank loan promptly after the completion of the merger. They contend, therefore, that arm's length bargaining would have produced a more favorable ratio for Susquehanna without precluding the likelihood that Gypsum's shareholders would have approved of the merger on different terms. The district court found this argument unpersuasive, but we cannot say that it is so lacking in evidentiary support that it does not warrant consideration by the trier of fact.

Accordingly, we conclude that there is evidence in the record from which a jury might find (1) that material facts were misstated or omitted from the proxy materials in violation of federal law; (2) that the violation caused the shareholders of Susquehanna to approve the merger on the terms submitted; (3) that terms which would have been more favorable to Susquehanna might have been sufficiently attractive to the Gypsum shareholders to make it reasonable to conclude that they would have given their approval to different terms; and (4) that the record contains relevant data from which a jury might make a just and reasonable estimate of the amount of Susquehanna's damage. We, therefore, hold that plaintiffs are entitled to have a jury decide the issues raised in their claim for damages predicated on the merger.

IV.

In our opinion, plaintiffs' remaining claims are all equitable in character. Two relate to the merger and three to Korholz's original purchase in May.

With respect to the merger, plaintiffs prayed that it either be set aside or that an independent arbiter be appointed to redetermine the exchange ratio. The record makes it quite clear that neither of these forms of relief would be feasible or appropriate. The merger itself (as opposed to its terms) does not appear to have harmed Susquehanna or its shareholders, and it is far too late to permit an arbiter to remake the bargain which the minority shareholders of Gypsum accepted.

With respect to the sale of 430,000 shares to Korholz, plaintiffs advance three theories of recovery, each of which is predicated on a version of the transaction which the district court rejected. Plaintiffs argue that certain findings with respect to the alleged transfer of control from Lannan and his associates to Korholz are clearly erroneous, or at least could be shown to be erroneous if admissible evidence had not been improperly excluded. For purposes of considering these claims, we assume, without deciding, that the evidence should have been received and that plaintiffs' version of the transaction is essentially correct.

They contend that Korholz's payment of $6,450,000 was not merely a purchase of shares but included the payment of a premium of about $1,075,000 to obtain working control of Susquehanna. He would not have paid that price unless he had been sure of adequate representation on the board, including election as its chairman. After his election, his position, coupled with his stock ownership, enabled him to exercise "working control" of the corporation. Assuming these facts as proved, we consider plaintiffs' three theories of recovery.

A. First, relying on *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833 (2nd Cir. 1968), *cert. denied*, 394 U.S. 976, plaintiffs contend that Rule 10b-5 was violated when the Lannan directors sold their shares on the basis of "material inside information" which they possessed and which they had a duty to disclose to the public. The inside information was the fact that Korholz had offered to pay them $15 per share for a block of 430,000 shares.

We would agree that if the directors, having knowledge of such an offer, had purchased shares at a lower price on the open market in order to assemble a block to be sold to Korholz at the premium price, those purchases on the open market would be securities transactions covered by Rule 10b-5. We find no evidence of any such purchases; nor is there any evidence that the plaintiffs, or any member of the class they represent, engaged in any purchase or sale of Susquehanna stock which would have been more favorable if the Korholz offer had been disclosed before his purchase from Lannan was consummated, or that anyone failed to engage in any favorable transaction as a result of the nondisclosure.

We do not believe Rule 10b-5 imposes an obligation on controlling shareholders to make prompt disclosure of every offer they receive[49], and find no evidence that an earlier disclosure of the Korholz offer would have benefitted plaintiffs in any way. We, therefore, conclude that the district court correctly rejected plaintiffs' first contention.

B. Plaintiffs also contend that the Lannan directors did not make an adequate investigation of Korholz before electing him to the board. They argue that a full investigation would have revealed that he was purchasing the stock on behalf of Gypsum, that he was already planning a merger, and that as a consequence of the merger Susquehanna would provide the funds which were used to pay $6,450,000 to the Lannan group.

To the extent that this argument is advanced to support the prayer that Korholz's election as a director should be declared null and void, it is foreclosed by findings of fact to the effect that adequate investigation of his character, reputation, and experience was made. Those findings are supported by the record.

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[49] "An insider's duty to disclose information or his duty to abstain from dealing in his company's securities arises only in 'those situations which are essentially extraordinary in nature and which are reasonably certain to have a substantial effect on the market price of the security if [the extraordinary situation is] disclosed.' Fleischer, Securities Trading and Corporate Information Practices: The Implications of the Texas Gulf Sulphur Proceeding, 51 Va.L.Rev. 1271, 1289." *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 848 (2nd Cir. 1968), *cert. denied*, 394 U.S. 976.

"The essence of the Rule is that anyone who, trading for his own account in the securities of a corporation has 'access, directly or indirectly, to *information intended to be available only for a corporate purpose* and not for the personal benefit of anyone' may not take 'advantage of such information knowing it is unavailable to those with whom he is dealing,' *i.e.*, the investing public. Matter of Cady, Roberts & Co., 40 S.E.C. 907, 912 (1961)" *Id.* (emphasis added.)

The information which some of the directors had — that Korholz was willing to pay $15 a share for 430,000 shares of Susquehanna stock — was not "information intended to be available only for a corporate purpose."

To the extent that the argument relates to the consequences of the merger, we believe it is subsumed by plaintiffs' second damage claim. If neither the merger itself nor its terms damaged Susquehanna, the fact that assets of the merged enterprise were used to discharge a liability of the merged enterprise certainly did not damage either of its components.

C. Finally, in their reply brief plaintiffs have directed our attention to *Keeley* v. *Black*, 107 A. 825 (N.J. Ch. 1919), and certain other state cases to support the suggestion that the premium received by a director in connection with the sale of a controlling block of stock should be treated as an asset of the corporation. The rule of that case is not a matter of federal law or, so far as we have been advised, the law of the state in which either Susquehanna or Gypsum was incorporated. Even if Lannan's shares constituted control of Susquehanna, we believe he had a right to sell them for a premium price. See *Essex Universal Corp.* v. *Yates*, 305 F.2d 572 (2nd Cir. 1962).

Defendants Lannan, Lauhoff and Schmick are not responsible for actions taken by other defendants or by the board of directors after their respective resignations. The death of defendant Michels has been suggested of record. Accordingly, insofar as the district court judgment dismissed the claims against Lannan, Lauhoff, Schmick and Michels, it is affirmed. As to the other defendants, the judgment is reversed and the case is remanded for a jury trial.

A true Copy:
Teste:

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Clerk of the United States Court of Appeals for the Seventh Circuit.

APPENDIX B

Memorandum Opinion

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 65 C 1757

WILLIAM DASHO, DASHO-ROGERS, INC., an Illinois corporation, and MAURICE H. SCHY,

Plaintiffs,

vs.

THE SUSQUEHANNA CORPORATION, a Delaware corporation, RALPH A. BOGAN, JR., EDWARD O. BOSHELL, M. M. HARDIN, HERBERT F. KORHOLZ, J. PATRICK LANNAN, HOWARD J. LAUHOFF, A. D. MARTIN, J. EARLE MAY, HUGH C. MICHELS, AKSEL NIELSEN, D. W. REEVES, R. C. SCHENK, FRANKLIN B. SCHMICK, HAROLD C. STUART, ALBERT W. THOMSON, FRANCIS C. WOOLARD and AMERICAN GYPSUM CO., a New Mexico corporation,

Defendants.

FINDINGS OF FACTS AND CONCLUSIONS OF LAW

This is a two-count action arising under the Securities Act of 1933 and the Securities Exchange Act of 1934. Count I of the complaint is an action under section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q; section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j; and Rule 10b-5 of the Securities and Exchange Commission promulgated under section 23(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78w. Jurisdiction is conferred upon this court by section 22(a) of the Securities Act of 1933, 15 U.S.C. § 77v, and by section 27 of the Securities Exchange

Act of 1934, 15 U.S.C. § 78aa. In this count plaintiffs, shareholders of the The Susquehanna Corporation (Susquehanna), have sued derivatively for injunctive relief and damages. In essence, they charged that prior to March 25, 1965, thirteen individual defendants, hereinafter referred to as the "Lannan Group" entered into a conspiracy with defendant H. F. Korholz, under which they, upon election as directors of Susquehanna, would sell or cause to be sold to Korholz 435,000 shares of Susquehanna stock for $6,525,000, a sum alleged to be $1,740,000 in excess of the fair market value of such shares, and then pass control of said corporation to Korholz through planned resignation and election of directors. Upon accomplishing this result, it was alleged, Korholz, as a part of the conspiracy, transferred the aforesaid shares to the American Gypsum Co. (Gypsum), in connection with which said company incurred a bank loan for substantially all of the purchase price. Thereafter, it was asserted, Korholz caused the Board of Directors of Susquehanna to approve a merger of the two companies, under which Susquehanna assumed the bank loan, and, in effect, acquired the 435,000 shares at the excessive price. This, plaintiffs contend, constituted a fraudulent sale of securities to Susquehanna, and, derivatively, to them, in violation of the aforesaid statutes. Further, it was alleged, in Count I, that the defendants herein, under threat of a shareholder's derivative suit by a Kansas City group, caused Susquehanna to transfer in May, 1965, 140,000 shares of common stock of Vanadium Corporation of America (Vanadium or VCA) to said shareholders for a price, paid in Susquehanna stock and boot, $700,000 less than its true market value. By causing such sale to be made, without disclosing the threatened derivative suit, it is alleged, defendants further violated Section 17(a) and Section 10(b).

Count II of the complaint is an action under section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C.

§ 78n; Rule 14a-9 of the Securities and Exchange Commission promulgated under Section 23(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78w; and section 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc(b). Jurisdiction is conferred upon this court by section 27 of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa. In Count II, plaintiffs alleged that in furtherance of the aforesaid scheme defendants caused Susquehanna to disseminate a false proxy statement in violation of Section 14(a) of the 1934 Act, 15 U.S.C. § 78n, and S.E.C. Rule 14a-9. Allegedly, this unlawful statement led to stockholder approval of Susquehanna's merger with defendant Gypsum, a New Mexico corporation.

This court originally sustained defendants' motion to dismiss this action. *Dasho* v. *Susquehanna* Corp., 267 F. Supp. 508 (N.D. Ill. 1966). That decision was reversed. *Dasho* v. *Susquehanna Corp.*, 380 F.2d 262 (7th Cir. 1967), cert. denied 389 U.S. 977 (1967). Subsequently, plaintiffs' demand for a jury trial was denied, and this cause was tried by the court. The court heard oral testimony, documents were received in evidence, and counsel for all of the parties argued orally and presented memoranda on behalf of their respective clients.

At the opening of trial, plaintiffs dismissed from the case defendants Mason, Wirtz, and Bard on the stated grounds that they did not attend the annual stockholders' meeting on April 19, 1965, and held small amounts of Susquehanna stock.

All of the individual defendants are reputable businessmen, the integrity and veracity of whom was not questioned on this record. All defendants except two were voluntarily produced by defense counsel as witnesses for plaintiffs' direct case. The only individual defendants who did not testify were Nielsen, whom plaintiffs' counsel excused on his own motion prior to Nielsen's scheduled testimony, and Michels whose testimony was admitted by stipulation. All of the defendants who testified were examined extensively as adverse witnesses by plaintiffs' counsel, and five other former officers, employees, or counsel for Susquehanna were called by plaintiffs and testified. Defendants rested their case without calling any witnesses.

The court, having considered all of the foregoing and being fully advised in the premises, finds as follows:

FINDINGS OF FACT

1. At the time the complaint was filed, plaintiffs owned 1900 shares of common stock of Susquehanna, a Delaware corporation, and they are presently Susquehanna shareholders.

2. Plaintiff Schy purchased 2,883 shares of The Susquehanna Corporation (Susquehanna) stock between July 1, 1963, and October 1, 1965, at an aggregate cost of $27,166. Between July 24, 1964, and April 24, 1967, he sold 2,783 shares at an aggregate consideration of $37,790.44; 1,000 of these shares were sold starting in December, 1965, after the merger of Susquehanna and American Gypsum Company (Gypsum). At the time of trial, Schy owned 100 shares.

3. Plaintiff W. A. Dasho acquired 501 shares of Susquehanna between January 25, 1963, and January 22, 1964, at a cost of $4,834.84. On November 28, 1967, he sold 100 of these shares at $42 each for an aggregate of $4,200. On October 28, 1968, when he already owned 401 such shares, Dasho acquired 400 shares of Susquehanna common stock. Seven hundred of these shares were sold in February and March, 1969. At the present time Dasho owns 117 shares of common stock of Susquehanna.

4. Plaintiff Dasho-Rogers, Inc. acquired 1,050 shares of Susquehanna between October 16, 1959, and January 5, 1962, at a cost of $17,974.39. Dasho-Rogers sold 900 shares in November and December, 1967, at an aggregate consideration of $37,450, at prices ranging between $41.125 and $42. Dasho-Rogers now owns 150 Susquehanna shares.

5. Susquehanna was incorporated in Delaware in 1953. Its principal place of business was Chicago, Illinois. On June 30, 1965, Susquehanna had outstanding 2,763,035 shares of $1.00 par value stock owned by approximately 8755 stockholders. The stock was traded over-the-counter.

6. In 1965, Susquehanna's principal operations were concerned with the operation of a uranium processing mill and mining properties. At this time two of the three existing plants supplying ore to the United States Atomic Energy Commission (AEC) under contracts expiring in 1966 had been closed down. A sulphuric acid plant, a vanadium facility, and a lightweight aggregate plant were operating. Former transportation operations had been cut to limited bus company operations. Since 1960 operating income decreased from $1,681,251 to $495,368 in 1964, and net income before Federal income tax from $751,168 to $404,750. At the same time the current assets of Susquehanna had been increasing, largely due to the sale of abandoned railway assets. Thus, current assets alone increased from $10,705,000 at the end of 1964 to $13,730,081 at the end of June, 1965. This last figure was approximately fifteen times current liabilities of $917,331.00. This increase was almost exclusively attributable to the cash realized from the sale of abandoned railway assets. As of June 30, 1965, Susquehanna's assets aggregating $27,598,446 consisted principally of current assets, an investment in the common stock of VCA carried at original cost of $2,925,768, and $4,491,249 in properties, plants, and equipment, approximately half of which represented abandoned railway assets at estimated salvage value.

6. As the result of the abandonment of its railroad properties in mid-1963, Susquehanna had available to it in 1964 approximately $12 million in a net operating loss (NOL) carry-forward. Under Internal Revenue Service Regulations, the losses could be carried over for five years from 1963, to offset any earnings during that period, and, to the extent not utilized, would expire at the end of 1968. With net income of only $1,527,489 for calendar year 1964, Susquehanna was faced with the probability of losing these tax credits unless a merger with, or acquisition by, another company with greater taxable earnings could be effected. Further, as the result of liquidation of real estate formerly connected with railroad operations, Susquehanna at the end of 1964 had available to it approximately $8 million in cash and certificates of deposit, all of which cash could be used in a merger with a company with more extensive operations than Susquehanna.

7. Plaintiffs sued on behalf of Susquehanna, for themselves, and for other shareholders similarly situated. Plaintiffs made no demand upon the officers or directors of Susquehanna to bring this action. It arose out of wrongs allegedly committed by Susquehanna management and a demand would have been unavailing.

8. The Complaint, as amended to the date of trial, named two corporate and 19 individual defendants. Thirteen of the individuals had served as directors of Susquehanna prior to the annual stockholders' meeting held April 19, 1965, when they were all re-elected (George J. Bard, Ralph A. J. Bogan, Jr., Edward O. Boshell, J. Patrick Lannan, Howard J. Lauhoff, Harold G. Mason, J. Earle May, Hugh C. Michels, R. C. Schenk, Franklin D. Schmick, Harold C. Stuart, Arthur M. Wirtz, and Francis M. Woolard). Two of these nineteen individuals also were elected as directors for the first time at that meeting (A. D. Martin and Albert W.

Thomson). Subsequent to that meeting, five of the directors elected April 19, 1965, resigned (Bard, Lannan, Lauhoff, Schmick, and Wirtz.) Four of these vacancies were filled by the remaining individual defendants (M. M. Hardin, Herbert F. Korholz, Aksel Nielsen, and Dick W. Reeves).

9. During the year preceding April 19, 1965, Susquehanna was managed by Messrs. Bard, Bogan, Boshell, Lannan, Lauhoff, Mason, May, Michels, Schenk, Schmick, Stuart, Woolard and Wirtz. The office in Susquehanna held by each of the aforementioned persons and the shares of Susquehanna which, on April 19, 1965, each member beneficially owned, are as follows:

Name	*Office*	*Shares of Susquehanna Owned or Controlled*
J. Patrick Lannan	Chairman of the Board of Directors, President and Director	174,659
R. C. Schenk	President and Director	2,147
Harold G. Mason	Vice President	100
George M. Bard	Director	3,000
Ralph A. L. Bogan, Jr.	Director	56,152
Edward O. Boshell	Director	16,212
Howard J. Lauhoff	Director	25,390
J. Earle May	Director	49,030
Hugh C. Michels	Director	73,061
Franklin B. Schmick	Director	11,233
Harold C. Stuart	Director	6,475
Arthur M. Wirtz	Director	2,038
Francis C. Woolard	Director	16,800
	Total Shares	438,297

10. In 1965 Gypsum was a New Mexico corporation with its principal place of business in Albuquerque, New Mexico.

The Chairman of its Board since 1962 was Hardin, who was one of the founders of Gypsum in 1959. Its President and Chief Executive Officer in 1965 was Korholz, who had come to Gypsum in 1962 as the result of a merger between Gypsum and Better Industries, Inc. In May of 1965 Korholz owned and controlled approximately 58% of Gypsum's common stock. The common stock was traded in the over-the-counter market. On June 30, 1965, issued and outstanding capital stock consisted of 86,752 shares of 6% cumulative preferred stock, par value $3, and 2,615,726 shares of common stock, par value $1.

11. Since 1958 and until May 18, 1965, the Chairman of the Board and Chief Executive Officer of Susquehanna was J. Patrick Lannan.

12. During late 1963 and all of 1964 Susquehanna actively pursued a program of seeking a partner in a "downstream" merger or acquisition, under which Susquehanna would acquire a smaller company and survive the transaction. At the end of 1964 and the beginning of 1965, due to Board dissatisfaction with the lack of success of this program, this policy was changed to one under which an "upstream" merger was being sought with Susquehanna not surviving the transaction. Defendant Schenk, then President of Susquehanna, Edward O. Boshell, Jr. (hereafter Boshell Jr.), son of defendant Boshell, and Ivan Bowen, III, a Vice President and Director, actively engaged in these activities. Although Bowen left Susquehanna in February 1965, acquisition activities continued under Schenk and Boshell Jr. By April 1965 at least one hundred companies had been investigated by them. All during 1964 and through May, 1965, the Board continuously discussed acquisition and merger possibilities brought to its attention by Lannan, Schenk, Bowen, and Boshell Jr.

13. On March 15, 1965, Susquehanna issued its annual report for 1964. On the same date a group of Kansas City stockholders of Susquehanna representing about 300,000 shares, headed by M. C. Coen, a stockholder, demanded from Susquehanna its list of stockholders. The Executive Committee of the Board on March 23, 1965, amended the by-laws of Susquehanna to increase the Board from twelve to fifteen members and authorized a management slate of such number of directors for consideration at the annual stockholders' meeting. This action was ratified by the full Board on March 26, 1965. Coen earlier in 1965 had sought to purchase about 250,000 Susquehanna shares at $12-13 per share and then had demanded three seats on the Susquehanna Board.

14. On March 25, 1965, the Susquehanna management proxy material was sent to Susquehanna stockholders. A management slate of fifteen members was proposed, consisting of Bard, Bogan, Boshell, Lannan, Lauhoff, May Michels, Schenk, Schmick, Stuart, Wirtz and Woolard, all of whom had been elected as directors at the 1964 stockholders' meeting, and three other officers of Susquehanna, including Mason. In a letter accompanying the proxy material, Lannan and Schenk stated that

> "As announced on March 15th by the Company, an outside group headed by 'Mike' Coen, a stockbroker from Kansas City, Missouri, and including . . . A. D. Martin of Dallas, Texas, has formally requested a list of Susquehanna stockholders for the purpose of soliciting proxies. Your management believes this action, through which the group may be seeking to gain control of the Company, to be a distinct disservice to Susquehanna stockholders, especially at a time when the financial strength of your Company has never been better. Furthermore, any attempt by

> outside interests to interfere with the management would seriously hamper merger negotiations now in progress with several major corporations whose stocks are listed on the New York Stock Exchange.
>
> The intentions of this outside group are not in the best interests of Susquehanna shareholders. If you do not intend to be present at the annual meeting, you are respectfully urged to sign, date and mail the enclosed proxy immediately. Your prompt attention to this matter will eliminate any possibility of this outside group disrupting the sound progress which has been made during the past twelve months. Do not execute any other proxy which may be offered for your signature."

Further proxy materials, largely dealing with the efforts of Coen in response to a card mailed to the stockholders by Coen on March 29, 1965, were mailed by management to Susquehanna stockholders on April 8 and 13, 1965.

15. At the stockholders' meeting held April 19, 1965, by cumulative voting, the twelve incumbent directors and Mason were elected, together with two nominees of Coen, defendants Martin and Thomson.

16. As of March 15, 1965, and thereafter through the annual stockholders' meeting on April 19, 1965, serious discussions with a view to merger or acquisition were being held by Susquehanna with companies the stocks of which were listed on the New York Stock Exchange. Possibilities included Borden Company, Commercial Solvents Corporation, Occidental Petroleum Company, Gulf Oil Company, W. R. Grace & Company, Christiana Oil Company, American Export Lines, and Pittsburgh Plate Glass Company. Following the stockholders' meeting, negotiations with American Export became more intensive.

18. As of the date of the stockholders' meeting and prior to the election of Korholz and two other Gypsum directors to the Susquehanna Board, there were no negotiations pending between Susquehanna and Gypsum concerning a merger of the two corporations. The acquisition of a large block of Susquehanna stock was not discussed until early May, 1965. In 1962 Korholz had visited Susquehanna's light-weight aggregate plant in California, at the request of its management. Thereafter, no contacts occurred between Korholz and Lannan on any business matter. In late December, 1964, Korholz apparently met socially with Lannan in New York. Early in 1965 Korholz mentioned to Boshell on at least two occasions that he might be interested in exploring merger possibilities with Susquehanna. Korholz was discouraged from doing so by Boshell because of other merger discussions by Susquehanna. Finally, in March, 1965, Boshell consented to put Korholz in touch with Schenk and Boshell Jr., the latter not an officer but an employee of Susquehanna.

19. On March 24, 1965, Korholz met with Schenk and Boshell Jr. in Chicago. The discussion related to the possibility of Susquehanna's acquisition of Gypsum. Certain published financial information was exchanged. No exchange ratio was discussed. Neither party regarded the discussion as having any importance, Korholz leaving almost immediately thereafter for Europe. The discussion never was resumed. As was his habit after all such discussions and as he had done on numerous occasions in 1964-65, Boshell Jr. prepared some preliminary statistical work showing a possible combination between Susquehanna and Gypsum, with an exchange ratio of 1.5 shares of Gypsum for 1 share of Susquehanna. This computation was not distributed to any other person by Boshell Jr.

20. Prior to May, 1965, no agreement, informal or formal, was made by any two or more of the defendants for

a merger between Susquehanna and Gypsum, for the sale of a large block of Susquehanna stock to Korholz or Gypsum, or for the resignation of any Susquehanna director. No conspiracy to effect these aims existed at any time either before or after March 25, 1965.

21. The proxy materials sent out by Susquehanna management with regard to the April 19, 1965, stockholders' meeting did not contain any material misrepresentations or omissions. The management nominees intended to serve their terms when elected. Susquehanna stock was not registered under the Securities Exchange Act until July 2, 1965.

22. Aware of publicity concerning the election of Thomson and Martin as dissidents to the Susquehanna Board at the April 19, 1965, stockholders' meeting, Korholz on May 3, 1965, met with Bogan in Chicago. Prior to that date there were no discussions or plans by Korholz to acquire shares of Susquehanna. At that meeting Korholz indicated that he was willing to offer $14 per share for a block of Susquehanna stock of approximately 300,000 to 400,000 shares, to include the approximately 112,000 shares held by Lannan and to be financed through First National Bank of Boston. At the meeting Bogan informed Korholz of an informal offer for Susquehanna shares received earlier that spring. Bogan agreed to contact Lannan concerning Korhloz' interest.

23. Late on May 3 or on May 4 Bogan communicated to Lannan by telephone Korholz' interest in acquiring a block of Susquehanna stock. Bogan also talked to William Brown, Vice President, The First National Bank of Boston, and ascertained that the requisite financing was available to Korholz. In New York Korholz conferred with Hardin, Chairman of the Gypsum Board, and with Boshell, who

agreed to remain on the Susquehanna Board. Korholz then went to Boston to talk with Brown about the financing. After his return to New York on May 5, Korholz again conferred with Boshell and Hardin concerning the purchase of the shares. Korholz requested that Bogan meet with him in Chicago on May 6. At no time was there any conversation or correspondence between Korholz and Lannan.

24. The meeting requested by Korholz was held on the evening of May 6 at the Chicago Airport. Bogan and Melvan Jacobs, an attorney, were present with Korholz. Korholz offered to pay $15 per share for Susquehanna stock and expressed a desire to be elected Chairman of the Susquehanna Board if the transaction was consummated. On May 7 or 8 Lannan indicated to Bogan his willingness to accept $15 per share for his shares and his desire to resign from the Board. Lannan stated that it was up to the Board to decide whether or not to elect Korholz as a director and Chairman of the Board. The election of Thomson and Martin as dissidents on the Susquehanna Board on April 19, 1965, and their actions at the ensuing Board meeting had discouraged Lannan. As Lannan told Bogan, "I am tired. I've had it." However, Lannan did not decide to sell his shares in Susquehanna until after Korholz' offer had been conveyed to him in early May.

25. Bogan immediately commenced to assemble a block of stock, for an off-the-market transaction, which procedure is routine in the investment banking business. Bogan contacted members of the Board of Susquehanna who held or represented substantial numbers of shares, with a view to assembling the block as expeditiously as possible. When contacted by Bogan, Lauhoff, Wirtz, and Schmick stated that they would sell their shares and wanted to and would resign from the Board of Directors. By May 17, 1965, Bogan has assembled a block of approximately 430,000 shares. Substantially all of the shares were processed by

the Jacobs' law firm for delivery to the Boston banks [sic]. Over 90 different stockholders sold shares as a part of the block.

Of the Susquehanna directors, Boshell, Stuart, Schenk, Woolard, Michels, and Bogan did not then sell any shares. Thomson and Martin were not contacted and did not sell either. May did not sell any of his personally owned shares but did loan some of his shares temporarily to some of his customers in order that they could deliver shares immediately to Jacobs.

26. On May 11, 1965, Korholz met again in Chicago with Bogan and Jacobs to work out what Jacobs described as the "mechanics of closing." By that date Bogan had been informed, and Korholz was advised, that Lannan, Wirtz, Schmick, and Lauhoff voluntarily were resigning from the Susquehanna Board. No request for these resignations was made by Lannan, Bogan, or any other Susquehanna official. Bogan and Jacobs insisted, and Korholz understood, that Korholz' desire to be elected Chairman in place of Lannan, and the filling of the other vacancies by Gypsum directors, were matters solely for the Board to decide, even though such elections became a condition requested by Korholz before the shares would be acquired. Susquehanna directors recognized that the remaining directors could fill any vacancies on the Board and that the owner of the 430,000 shares would have the right to elect such number of directors by cumulative voting at a special meeting of the stockholders.

27. The written offer to purchase made by Korholz to the selling Susquehanna stockholders, executed by Korholz May 14, contained provisions that the transaction would not be consummated unless a specified number of shares of Susquehanna was deposited in an escrow at the First National Bank of Boston, that certain directors submit their resignations

from the Susquehanna Board, and that certain other individuals be elected to fill the vacancies created thereby. Under the escrcw agreement between Korholz, Jacobs (as attorney for the selling stockholders), and the Bank, payment for the shares deposited could not be made by the Bank unless and until Korholz and Jacobs jointly instructed the Bank, by no later than 4 P.M., May 19, 1965, that all conditions had been fulfilled and that the funds could be disbursed.

28. The offer to purchase and the escrow agreement did not constitute a written understanding to sell or deliver any such directorship. Until a Board meeting was held and the directors acted, the offer and the escrow agreement documents could not be effective. There was no assurance that the conditions would be met. Not until Korholz and Jacobs, after the conditions had been met on May 18, 1965, by action of the Susquehanna Board, jointly instructed the Bank to disburse the funds, could the selling stockholders receive cash for their shares. Bogan had informed the selling stockholders that there was no assurance that their stock would be sold when deposited for sale. No public announcement of the sale, or of the resignation and election of directors, could have been made until the Board met and acted on May 18, 1965, and the joint instruction to the Bank was given. Until that time, it was possible that the conditions would not be met, that the sale would not be effectuated, and that Korholz, Hardin, and Nielsen would not be elected to the Susquehanna Board.

29. There never existed any oral or written understanding or agreement to deliver control of Susquehanna to any buyer. Lannan's personal stockholdings of approximately 112,000 shares did not constitute a "control" block of stock. Woolard, Bogan, and May, who were not selling their shares, owned or could influence more shares, through their investment banking firms, than could Lannan. The Susquehanna

directors who were elected on April 19, 1965, many of whom testified at this trial, were not controlled by Lannan or any other officer or director of Susquehanna. They exercised an informed, independent business judgment before and after the change in Susquehanna management in late May, 1965. The same is true of the three new directors (Nielsen, Reeves, and Hardin) who went on the Susquehanna Board with Korholz in May and June, 1965. Indeed, as a practical matter, these four persons did not even constitute a majority of the Board of fourteen members. No director was ever elected to fill the vacancy of Bard, whose resignation was accepted on July 15, 1965. Nothing in this record establishes that the approximately 15% of the outstanding and issued stock of Susquehanna represented by the 430,000 shares, either in the hands of, or subject to the influence of, the Susquehanna directors on April 19, 1965, or in the hands of any buyer at the end of May, 1965, representing control of the voting power of Susquehanna.

30. In May, 1965, Gypsum had loan agreements with Massachusetts Mutual Life Insurance Company (Massachusetts Mutual) and State Mutual Life Assurance Company of American (State Mutual). Under those agreements, before any bank loan for the purchase of Susquehanna shares by Gypsum could be obtained, the approval of those companies were required. Such approval was given between May 12 and May 14, State Mutual attaching as a condition that

> ". . . Herbert Korholz become Chief Executive Officer of Susquehanna Corporation; that he and two other directors of American Gypsum are to be elected Directors of Susquehanna Corporation and within 90 days will have the right to appoint two additional directors. . . ."

31. The Gypsum Board on May 12, 1965, authorized Korholz to acquire for Gypsum approximately 430,000 shares of Susquehanna stock at $15 per share.

32. On or before May 18, 1965, the directors of Susquehanna assumed that Korholz was acquiring the 430,000 shares as a personal investment. Korholz intended to acquire the shares as a corporate opportunity for Gypsum, with a view to possible merger between the two companies if all the requisite legal, financial, and evaluation steps required for such action could be taken. Pursuant to the action of the Gypsum Board, and because of delays in processing a loan for that corporation through the First National Bank of Boston and the two insurance companies, Korholz, in order to take advantage of the corporate opportunity for the benefit of Gypsum, agreed to loan his personal credit to Gypsum and borrow the necessary funds temporarily in order to acquire the shares for Gypsum. The necessary papers for the sale of 430,000 shares were prepared by the attorneys for the selling stockholders and First National Bank officials.

33. Prior to the May 18, 1965, meeting of the Susquehanna Board, investigation was made by Susquehanna directors concerning the backgrounds of Korholz, Nielsen, and Hardin. This matter was further developed at a luncheon meeting on May 18, 1965, in Chicago before the Board meeting. Reeves, who relunctantly joined the Susquehanna Board because of his other business interests, also was well known to the members who had been elected April 19 and who had remained on the Board after May 18. Full information was sought and received by the Board members concerning the business background, experience, and integrity of the four new directors.

34. At the Board meeting which followed, Boshell, Bogan, Lauhoff, Martin, Mason, May, Michels, Schenk, Schmick,

Stuart, Thomson and Woolard were present. Upon the acceptance by the Board of the Resignations of Lannan, Wirtz, and Lauhoff, their vacancies were filled by Korholz, Hardin and Nielsen, respectively. Korholz was also elected as Chairman of the Board and a member of the Executive Committee, and Nielsen a member of the Executive Committee. Schmick's resignation was accepted by the Board on June 18, 1965, and Bard's resignation on July 15, 1965. Reeves was elected to the vacancy of Schmick at a Susquehanna Board meeting on June 18, 1965, but the Bard vacancy never was filled. Subsequent to the dates of their resignations, Lannan, Wirtz, Lauhoff, Schmick, and Bard had nothing to do with the affairs of Susquehanna in any capacity whatsoever.

35. Immediately after the May 18, 1965, meeting and only upon joint telephone instructions by Korholz and Jacob to the Bank, the latter proceeded to disburse the funds loaned in the amount of $6,450,000. The stock was placed in escrow by May 20 and paid for May 25, 1965. Over 90 Susquehanna shareholders, many of whom were not known to Lannan, participated in the transaction. The loan was formally assumed by Gypsum on July 2, 1965. The acquisition by Korholz of 12,500 shares of Susquehanna from Wheelock Whitney, a former Susquehanna director, in August, 1965, pursuant to a "put" granted by Korholz on May 18, 1965, was not involved in the 430,000-share transaction and was a purely personal transaction unrelated to the issues in this suit.

36. Two of the directors of Susquehanna, Boshell and Stuart, suggested to some of their colleagues on May 18, 1965, that consideration should be given to making a general tender, pro rata, to all Susquehanna stockholders for the 430,000 shares. However, neither Boshell nor Stuart considered the method used in assembling the shares illegal or a breach of any fiduciary duty by the directors to the stockholders. Testimony of knowledgeable witnesses in the se-

curities field, as were several of the defendants, established that a general tender for 430,000 shares, pro rata, would have been impracticable. Even more impracticable would have been a general tender offer for up to 51%, or all, of Susquehanna's outstanding stock. The market price of Susquehanna would have gone up very rapidly. At least six months would have been required to assemble the shares which were widely held. Such a step would have lost for Susquehanna the advantages of the new management which every director remaining on the Board recognized were needed by the corporation. In effect, a corporate opportunity would have been lost, and all of the stockholders thus adversely affected.

37. Further, the negotiations between Korholz and Bogan and Jacobs were not that type of material information which could or should have been released to the public and other stockholders. This was because the information concerned only an expectation and was wholly speculative until the Susquehanna Board met on May 18, 1965, and took certain action. Absent such a meeting and action, the Korholz offer could not become a reality. Release of such premature information prior to May 18 might have adversely affected the market price of Susquehanna itself. No evidence whatsoever was offered by plaintiffs that prompt, timely, and proper publicity was not released concerning the sale of Susquehanna shares or the Board resignations and elections. Such evidence is required to establish lack of proper disclosure. No such evidence was so offered by plaintiffs, who had the burden of proof.

38. As it was, when the information as to facts was publicly released promptly after the May 18 Board meeting, there was no effect whatsoever on the price of Susquehanna in the over-the-counter market, as shown by the following quotations from the National Quotation Bureau,

	Bid			Asked		
1965	**High**	**Low**	**Average**	**High**	**Low**	**Average**
5/3	11⅞	11¾	11 13/16	12½	12	12¼
5/4	11⅞	11⅝	11¾	12⅛	12	12 1/16
5/5	11¾	11⅜	11 9/16	12	11⅝	11 13/16
5/6	11⅝	11½	11 9/16	11⅞	11¾	11 13/16
5/7	12¼	12	12⅛	12⅜	11⅞	12⅛
5/10	13¼	12¾	13	13⅝	13¼	13⅜
5/11	13½	13	13¼	13⅝	13⅜	13½
5/12	13	12⅝	12¾	13⅜	13	13⅛
5/13	13¼	13	13⅛	13⅝	13⅜	13½
5/14	13½	13¼	13⅜	13⅞	13⅝	13¾
5/17	13⅝	13⅜	13½	14	13¾	14
5/18	13¾	13⅛	13¼	13¾	13½	13¾
5/19	13½	12⅝	13	13¾	13⅛	13½
5/20	13¼	11⅝	12½	13¾	12⅛	13
5/21	12½	11⅝	12 1/16	12⅞	12⅛	12½
5/24	11⅞	11¾	11 13/16	12⅞	12⅛	12½
5/25	11⅞	11¾	11 13/16	12⅝	12⅛	12⅜
5/26	12	11¾	11⅞	12⅜	12⅛	12¼
5/27	12¼	11⅞	12 1/16	12⅜	12¼	12 5/16
5/28	12¼	12	12⅛	12½	12⅜	12 7/16
6/1	12⅜	12¼	12 5/16	12¾	12½	12⅝

These statistics clearly show that the movement of prices in Susquehanna during the month of May was orderly. Prices never moved more than one point upwards or downwards. Susquehanna never went as high as 15 at any time during 1965 after May 18. The high bid for this period was 13⅜ on October 20, when the high asked reached 13⅝. The next day the high asked reached 13¾, the highest for the last six and one half months of 1965. It was not until May 4, 1967, that Susquehanna stock (both high bid and high asked) exceeded 15.

39. The amount of $15 per share received by the Susquehanna shareholders for their 430,000 shares was reasonable,

was in accordance with normal rates for such a block, and yet could not assure control of Susquehanna. The amount received by the defendants who sold their shares was not so high as to indicate the possibility of a violation of any fiduciary duty these sellers may have had to the other stockholders of Susquehanna.

40. The negotiations for the sale of the 430,000 shares did not constitute a conspiracy or agreement to deprive the other stockholders of any valuable asset or profits to which they might be entitled. The negotiations were arms'-length, did not involve a sale of Susquehanna directorships for money, and did not involve the sale of control of Susquehanna by the resigning directors to Korholz and the other three new Susquehanna directors. In electing Korholz, Hardin, Nielsen, and Reeves to the existing vacancies, the directors of Susquehanna were fully informed and satisfied concerning their business background, experience, and integrity. No material inside information was involved in this private sale which was required to be disclosed to the other stockholders. When the information concerning the sale and changes in directors was released after the May 18, 1965, directors' meeting, there was no effect whatsoever on the over-the-counter market in Susquehanna common stock. The price paid to the selling stockholders was reasonable.

41. When Korholz became Chairman of the Susquehanna Board, three principal problems faced that corporation. The first was the litigation arising out of the Susquehanna investment in VCA common stock. The second arose from the presence of two dissident directors on the Board, elected by Coen. The third was what Korholz considered lack of "basic direction" in corporate management. This record establishes that the Susquehanna Board, with Korholz as Chairman, solved these problems.

42. Because of Susquehanna's interest in uranium and related minerals, Susquehanna acquired 140,000 shares of the stock of Vanadium Corporation of America (VCA), traded on the New York Stock Exchange, between November 7, 1960, and April 26, 1961, at an aggregate cost of $2,925,766 or $20.90 per share. Immediately thereafter, Susquehanna officials indicated to VCA management that Susquehanna desired to initiate merger discussions.

43. VCA management refused a proposed merger and instituted suit against Susquehanna in the Federal District Court in Delaware in January, 1962, alleging violation of the antitrust laws. On February 26, 1962, the Court entered an injuction *pendente lite,* as follows:

> "Until further order of this Court, defendants and each of them, their officers, agents, servants, employees, and attorneys, and all other persons acting by, on behalf of, or in concert with them or either of them, are jointly and respectively enjoined during the pendency of this action from directly or indirectly:
>
> "(a) Acquiring any additional shares of stock of plaintiff, unless the parties agree on a modus operandi via an escrow arrangement;
>
> "(b) Voting any shares of stock of plaintiff at any meeting of plaintiff's stockholders, or granting any proxy to vote any of said shares;
>
> "(c) Acquiring any representation, direct or indirect, on plaintiff's Board of Directors; or
>
> "(d) Taking any other action toward a merger, consolidation or other unity of interest between defendant, The Susquehanna Corporation, and plaintiff pendente lite."
>
> *Vanadium Corp. of America* v. *Susquehanna Corp.,* 203 F. Supp. 686, 697 (D. Del. 1962).

44. In March 1962, Susquehanna (through its subsidiary Susquehanna-Western, Inc.) was sued under the antitrust laws by Minerals Engineering Company in the Salt Lake City Federal District Court. The complaint was based in large part upon the findings of the Delaware Federal District Court.

45. Late in 1962 and in 1963 and 1964, contact was made by Susquehanna officials with VCA and its second largest stockholder, International Mining Company, with a view to settlement of the VCA litigation. In early 1965 settlement negotiations were conducted through counsel for both companies. This culminated in a meeting in April, 1965, in Chicago, attended by Schenk and counsel. At that meeting draft settlement papers were exchanged, and Susquehanna offered to sell its stock to VCA at the then market, which exceeded $20.90. A final draft of a settlement agreement was delayed because of the reservations of certain directors to the language presented at the May 18, 1965, meeting of the Board. A proposed settlement was authorized by the Board at its meeting on June 18, 1965, subject to changes or modifications as Korholz or Schenk might direct.

46. At the June 18, 1965, Board meeting, Thomson distributed to the Board a letter dated June 17, 1965, in which Coen demanded that suit be brought against the directors who sold their shares and that Korholz, Hardin, and Nielsen not be permitted to exercise their duties as directors. A similar letter dated May 28, 1965, had been sent by Coen to the Susquehanna directors but withdrawn by telegram on May 31, 1965. The June 17 letter was referred to Susquehanna counsel for study.

47. Following receipt of Coen's May 28, 1965, letter, Korholz contacted Coen who suggested that Korholz acquire at $15 per share the approximately 250,000 Susquehanna shares

held by Coen and customers of Coen's brokerage firm, Midwest Securities, Inc. Korholz was unable to arrange a loan to purchase these shares through First National Bank of Boston.

48. On June 22 and 23, 1965, Korholz met with Coen in Kansas City. The possibility of exchanging the 140,000 VCA shares for the Susquehanna shares held by Coen and his customers was discussed. On July 3, 1965, Korholz, who had been unable to meet with VCA's Chief Executive Officer in New York, informed the latter that the VCA shares were being sent to the Boston Bank pending their sale to a third party. VCA counsel advised that VCA would have no objection to a sale and would hold up litigation for the time being. Korholz reported a possible exchange of the VCA shares for Susquehanna shares to the Susquehanna Executive Committee on July 9, 1965. The matter was placed on the agenda of the full Board meeting to be held July 15, 1965.

49. At the July 15, 1965, meeting of the Susquehanna Board, its general counsel orally informed the directors that there was no substance to the claims made by Coen in his June 17, 1965, letter. Although Thomson, as counsel for Coen, drafted the letter for his client and believed at the time of its sending that the allegations possibly might be true, he acknowledged at the trial that the facts did not turn out to be those claimed and that therefore no cause of action existed against the Susquehanna directors. The allegations of the letter, in the light of Coen's prior attempt to take over control of Susquehanna, had the flavor of advocacy. Withdrawal of the June 17 letter on August 10, 1965, therefore was not unusual. Indeed, Martin continued to serve on the Susquehanna Board until April, 1966, when he was not a candidate for re-election at the 1966 annual stockholders' meeting.

50. The Directors on July 15, 1965, acting in good faith and exercising an informed, independent business judgment, au-

thorized the exchange of the 140,000 VCA shares for approximately 250,000 shares of Susquehanna, plus appropriate cash, on a "market-to-market" basis. The business and legal reasons dictating this course of action included the inability of Susquehanna to dispose of the VCA shares at a premium to any buyer, including VCA itself, and the substitution of Treasury shares or "acquisition currency" for what was in effect a frozen or "sterile" asset, without voting or any other rights. Susquehanna would not be forced to enter into a settlement agreement with VCA which required Susquehanna "forever" not to exercise these rights of ownership. The VCA litigation, set for trial in September, 1965, could be dismissed,[1] thus removing its usefulness to the Salt Lake City litigation.[2] Susquehanna earnings per share would be increased. The divisive influence on the Board represented by two directors might be removed, thus permitting Susquehanna to function more effectively and harmoniously.

51. The agreement was executed July 15, 1965. It was received and accepted by First National Bank of Boston on July 22, 1965. A suggestion that the agreement be revised was rejected by Thomson as Coen's counsel. On July 15, 1965, there was no understanding, agreement, or intention that the VCA shares would be resold by Coen, with or without the assistance of Korholz.

52. Late in July, 1965, Coen asked Korholz to help him to contact International Mining Company (IMC), which after Coen was the largest stockholder of VCA. Korholz knew, and introduced Coen to, Louis Harder, President of

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[1] The Court takes judicial notice that the case was dismissed in September 1965.

[2] The complaint had been filed March 9, 1962. The suit was settled in early 1966. *Minerals Engineering Co.* v. *Susquehanna-Western Inc.* and *The Susquehanna Corporation,* Civil Action No. C-46-62, U.S. District Court, District of Utah, Central Division.

IMC and a director of VCA. After this introduction, Korholz had nothing further to do with Coen's negotiations. Coen threatened to make a tender offer at $25 per VCA share in order to buy enough additional VCA shares to bring his holdings up to over 51%. VCA offered Coen and his group $24 and then $24.125 per share on August 3-4, 1965, obviously to prevent an attempted takeover by Coen. The median price for VCA stock on the New York Stock Exchange between July 14 and August 3, 1965, was $19.971.

53. On August 11, 1965, the VCA shares were exchanged for 222,107 Susquehanna shares plus cash of $300,685, representing an exchange price of $19.25 per VCA share and $10.78 per Susquehanna share. These were the market prices in effect on July 14, the last business day before the agreement was executed.

54. At the closing on August 11, 1965, Coen sold his VCA shares to VCA at $24.125 per share.

55. First Greystone Corporation was incorporated on September 13, 1965, as a Missouri corporation. The officers and directors included Coen and Thomson. The capitalization of First Greystone Corporation consisted of common stock and debentures, issued in two separate offerings. Korholz was not a Greystone stockholder in 1965. In February, 1967, Korholz paid cash to become a stockholder of First Greystone Corporation, holding 400 shares of common stock, and $15,000 of debentures. There is no support for plaintiff's allegations that Korholz received Greystone stock as a payoff by Coen for some favor allegedly rendered to Coen by Korholz in connection with the VCA stock transaction in July and August, 1965.

56. When he became Chief Executive Officer of Gypsum in 1962, Korholz sought to expand that company with ac-

quisitions. After 1962 Gypsum merged with Treesdale Laboratories, Inc., The Kelsey-Ferguson Brick Company, and Kelsey Company, largely due to the efforts of Korholz.

57. In 1965 Gypsum was engaged in the manufacture of gypsum wallboard, rock wool insulation and slag products, and exothermic products for the steel foundry industry, and in the mining and processing of perlite. During the period 1962 through the end of the fiscal year June 30, 1965, Gypsum net sales had increased from $14,862,181 to $20,222,996, and net income before taxes from $612,698 to $1,568,725. As of June 30, 1965, Gypsum's assets of approximately $22 million consisted principally of $7.9 million in current assets, $6.4 million in investments (principally its holdings of Susquehanna stock), and $6.9 million in plants and properties.

58. At its meeting on June 18, 1965, the Susquehanna Board of Directors appointed an Acquisition Committee to consider and act upon stock and security purchases, which, in the judgment of the Committee, would advance the merger and acquisition program of the Corporation. Bogan (Chairman), Boshell, and Korholz were elected to the Committee, Martin and Thomson voting in the negative. As [sic] amendment proposed by Martin and Thomson to prohibit the Committee from purchasing an interest in any company in which any member of the Board of Directors had an interest was rejected. In rejecting this motion, the Board believed that every precaution would be taken to prevent any member of the Board from directly or indirectly profiting from any acquisition made by the Acquisition Committee The amendment proposed by Martin and Thomson would not have been applicable to any merger discussions between Susquehanna and Gypsum, since Susquehanna purchased no securities of Gypsum prior to the merger.

59. After May 18, 1965, Susquehanna sought a "downstream" merger or acquisition, with Susquehanna the surviving corporation. Gypsum was not the only prospective partner considered during the last half of 1965. Stock of General Refractories Company and North American Refractories Company, among others, was purchased in the summer and fall of 1965, with a view to Susquehanna's making a tender offer for those companies. However, these efforts were unsuccessful.

60. Late in May, 1965, Bogan and Schenk visited Gypsum's plants. Commencing in late June, 1965, Boshell, with Korholz and Bogan present on two occasions, met with representatives of New York Hanseatic Corporation (New York Hanseatic) concerning the preparation of a report on the feasibility of a proposed merger between Susquehanna and Gypsum. On July 9, 1965, two representatives of New York Hanseatic presented an oral report to the Susquehanna Board Executive Committee, tentatively suggesting an exchange ratio of 1 share of Susquehanna for 1.8-1.9 shares of American Gypsum.

61. New York Hanseatic also presented a tentative report to the full Susquehanna Board at its meeting on July 15, 1965. The Board directed that New York Hanseatic submit a written report to the Acquisition Committee, that the latter Committee analyze and report on the matter to the full Board, and that the Committee select and retain an organization to undertake a separate, independent study and appraisal of Susquehanna to verify the report and conclusions of New York Hanseatic, which also had been retained by Gypsum. Stone & Webster was retained for this further study and appraisal.

62. Further merger discussions were held at the Susquehanna Board meeting on August 25, 1965. At the latter

meeting a New York Hanseatic recommendation of an exchange ratio of one share of Susquehanna for 1.9 shares of Gypsum was approved. After a study for the purpose of reaching their own conclusions, Stone & Webster concurred with New York Hanseatic. The Gypsum Board approved the merger on August 30, on the basis of both reports, which were made to the two proposed merger partners. The formal merger agreement between the two companies was approved by the Boards of Susquehanna and Gypsum on October 5 and 19, 1965, respectively.

63. Although plaintiffs from the outset of the trial stated that they would present expert evidence attacking the validity of the New York Hanseatic and Stone & Webster reports, such evidence never was presented. No credible evidence on this record challenges the factual premises and expert recommendations of those reports. Both organizations, particularly Stone & Webster, were in 1965 and are, nationally recognized, with the necessary expertise for merger evaluation. Plaintiffs have contended that the New York Hanseatic and Stone & Webster reports were tainted by prior associations between those organizations and officers and directors of Susquehanna and Gypsum but offered no evidence to support those contentions.

64. New York Hanseatic on one prior occasion in 1964 rendered an evaluation report to Gypsum concerning a merger between Gypsum and Treesdale Laboratories, Inc. Boshell served as an attorney and Financial Vice President for Stone & Webster between 1934 and 1948. Stone & Webster in 1961 rendered a report to both Susquehanna and VCA concerning a possible merger between the two companies. No further work was done by either company for Susquehanna or Gypsum until late June, 1965. Neither New York Hanseatic nor Stone & Webster had been an underwriter for Gypsum or Susquehanna. No recommendation or report to

Gypsum or Susquehanna was made by New York Hanseatic or Stone & Webster concerning the proposed merger or any terms thereof, prior to the report submitted to the Susquehanna and Gypsum Boards after June, 1965. Neither report was made to substantiate or back up an earlier recommendation to either company in connection with the rendering of investment banking services.

65. None of these facts justifies a finding on this record that the exchange ratio recommended by New York Hanseatic and Stone & Webster was, in any manner whatsoever, unfair to the stockholders of either corporation. An examination of the New York Hanseatic and Stone & Webster reports themselves demonstrates that the reports recommended an exchange ratio which was based on extensive studies of all available financial and business information.

66. In recommending a per share value of Susquehanna, New York Hanseatic found that Susquehanna's "break-up" value exceeded the worth that could be attributed to Susquehanna as a going concern. New York Hanseatic concluded that the total market value of the net assets of Susquehanna as of December 31, 1964, was approximately $27,135,000, which was equal to $10.75 per common share on the 2,524,788 shares then outstanding. On the basis of unaudited figures for the six months ended June 30, 1965 (published in the joint proxy statement), New York Hanseatic concluded that the total market value for the net assets was approximately the same. This conclusion was substantiated by Susquehanna's consolidated balance sheets, as of December 31, 1964 (audited), and June 30, 1965 (unaudited), prepared by Susquehanna's independent auditors and published in the joint proxy statement. These balance sheets showed the only material change in Susquehanna's assets between December 31, 1964, and June 30, 1965, was

a shift of approximately $3,000,000 from abandoned railway assets, at estimated salvage values, to total current assets.

67. Gypsum was evaluated as an operating business. In reaching a final value, New York Hanseatic capitalized earnings at a consetvative capitalization rate of 10. The capitalization of Gypsum's adjusted earnings of 56.5 cents per share with a multiple of 10 established a value of $5.65 per common share of Gypsum. As to this multiple, New York Hanseatic found that

> "American Gypsum Company has historically been valued in the market at 13 to 18 times recent 12 month earnings per share, consistently higher than the industry average price-earnings ratio of 13 to 14.5. . . . However, in view of the financial condition of the Company and the adjustments to reported earnings, it is our opinion that the appropriate capitalization rate which should be applied to the adjusted earnings is 10%. Applying this figure to the adjusted earnings of American Gypsum Company results in a value of $5.65 per common share."

The over-the-counter market place did not differ with the evaluation made by New York Hanseatic. The ratio of the average bid price of the common stocks of Susquehanna and Gypsum during the year 1964 ranged between 1.15 to 1 to 1.87 to 1 and for 1965 ranged between 1.76 to 1 to 2.02 to 1. The exchange ratio was reasonable in light of the intrinsic value of each company and the relative contributions of the two companies to the surviving corporation.

68. Among the more important factors considered by New York Hanseatic in determining the appropriate capitalization rate for Gypsum was an adjustment to the cost of the 430,000 shares, held by Gypsum, to the value of $10.75

per share (approximately equal to the market value at that date and to New York Hanseatic's estimate of the per share value of Susquehanna stock), and the $6,450,000 loan to acquire said shares.

69. Both New York Hanseatic and Stone & Webster found that the exchange ratio of 1.9 shares of Gypsum stock for one share of Susquehanna was fair and equitable to the stockholders of both companies. Korholz and Reeves believed that the ratio was fairer to Susquehanna than it was to Gypsum. However, both agreed to accept the ratio in reliance upon the expert opinions of New York Hanseatic and Stone & Webster. Pursuant to that ratio, when the merger became effective December 13, 1965, 2,615,726 shares of Gypsum common stock were exchanged for 1,274,734 shares of Susquehanna stock. The surviving corporation therefore, had 3,322,347 shares outstanding.

70. All of the directors called as witnesses by plaintiffs considered the merger fair and equitable to, and in the best interests of, the stockholders of Susquehanna. The merger meant a substantial increase in tax-free earnings, as well as net earnings, per share through the addition of Gypsum revenues. Utilization of the Susquehanna net operating loss also increased Susquehanna earnings. A more aggressive management group was added to Susquehanna. The merger permitted full utilization of the cash resources of Susquehanna and thus strengthened the financial position of the combined enterprise.

71. Plaintiffs claim Susquehanna was forced to buy back, directly or indirectly, the 430,000 shares sold by the selling stockholders to Gypsum, at a price of $15, $2 in excess of alleged true market value of the shares, thus looting Susquehanna of $6,450,000 in assets and property. Cash of Susquehanna, as the surviving corporation, was not used

to pay off the bank loan. The loan was liquidated in the late summer of 1968 out of the proceeds of an underwriting by Susquehanna by the sale of debentures.

72. Plaintiffs claim that the value of Susquehanna shares should have been computed on the basis of book value or values in excess of market ranging from $15 to $18. Book value generally is not considered a significant factor in determining merger ratios. The $15 value represented what Korholz and Gypsum considered the 430,000 shares to be worth in their hands, for which they were willing to pay a reasonable premium. Indeed, for purposes of the merger, the 430,000 shares, which became Treasury shares and thus "acquisition currency", and the bank loan of $6,450,000 were "wash" items, cancelling each other out on the balance sheet of the combined corporation.

73. Plaintiff offered no testimony to counter the expert opinions of New York Hanseatic and Stone & Webster. No merger evaluation can be perfect. The Court cannot and should not substitute its judgment for that of experts whose credentials and opinions are unchallenged on this record. The New York Hanseatic and Stone & Webster reports, and the testimony with respect to these reports, conclusively established that the merger was a good one for both companies and that the exchange ratio computed by these two well qualified experts was fair.

74. Susquehanna was not the victim of any looting or damage resulting from any looting. There is no proof whatsoever that funds of Susquehanna were diverted into the pockets of any defendant in this case. This Court in this case has found,

> "(t)he corporate health and strength of Susquehanna, as reflected by the increased size of its size of its assets and the increased market valuation of its stock,

> is not irrelevant to the *quality of Korholz' intent with regard to the corporation's assets, the director's duty of care in selecting new members of the Board,* and the real value of Gypsum stock." (Memorandum Opinion, Oct. 18, 1968, p. 6 on Plaintiff's motion to strike certain affirmative defenses of Defendants).

There is no question that, partly as a result of the merger with Gypsum, Susquehanna has become a more diversified national corporation. Its operations have been expanded to include a research organization (formerly Atlantic Research Corporation). Its business has grown from $17 million to $150 million. Its stock reached a high of $80 in 1968.[3] Since December 1967, Susquehanna's common stock has been traded on the American Stock Exchange.

75. A joint Susquehanna-Gypsum proxy statement was mailed November 15, 1965, to the stockholders of both corporations. On December 2, 1965, the plaintiffs in this case distributed to the Susquehanna stockholders proxy material, which urged the stockholders to oppose the merger. At the meeting of Susquehanna stockholders held on December 7, 1965, 2,106,206 shares, or 84% of all entitled to vote, were represented in person or by proxy, 1,866,870 shares, or 75% of the shares issued and outstanding, were voted in favor of the merger, and 164,000 shares, or 6.59% of such shares, were voted against the merger. The shareholders of Gypsum, at a meeting thereof on December 10, 1965, approved the merger by the affirmative vote of 2,317,568 shares out of 2,326,508 represented at the meeting (97% of all of the shares issued

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[3] The Court takes judicial notice of the finding of this Court concerning, as the result of a further merger at the end of 1967, "the corporate health and strength of Susquehanna." *Schy* v. *The Susquehanna Corporation et al.*, No. 67-C-1790. Findings of Fact and Conclusions of Law, December 17, 1968, Finding 14, pp. 8-9.

and outstanding and entitled to vote). The merger of Gypsum into Susquehanna became effective on December 13, 1965.

In the lengthy November, 1965, proxy statement concerning the proposed merger, over thirty different areas of information are shown in the table of contents. Every matter upon which the stockholders should have been informed, in order to make an intelligent decision with respect to the merger, was disclosed.

76. Evidence adduced by plaintiffs on this record establishes that Susquehanna's counsel supplied all information requested by the SEC Staff with respect to the proposed proxy statement. Procedures developed by the SEC for the processing of proxy material were fully complied with. This Court already has found that there was *prima facie* full disclosure to plaintiffs, 267 F. Supp. at 512.

77. The Proxy Statement (p. 4) stated:

> "On October 5, 1965, the Board of Directors of Susquehanna . . . unanimously approved the execution and delivery of the Agreement of Merger. . . . Four of the 14 directors of Susquehanna (including J. F. Korholz, Chairman of the Board of Susquehanna and President of Gypsum) are also directors of Gypsum."

There is no evidence that the foregoing are deceptive.

78. There is no necessity to disclose an alleged intention of Korholz to seize control of the corporation through the sale of corporate offices, because no sale of control through the sale of corporate offices occurred in fact.

79. There was no necessity to state that the acquisition of Susquehanna shares by Korholz followed a pattern used by him in Natco and Treesdale Laboratories, Inc. Natco had

nothing whatsoever to do with the proposed Susquehanna-Gypsum merger. Material details of the Treesdale-Gypsum merger were fully disclosed in the proxy statement.

80. That New York Hanseatic gave advice concerning one merger ratio for Gypsum in an unrelated transaction prior to the proposed Susquehanna-Gypsum merger is not material.

81. Susquehanna stock ownership of directors who were to serve on its Board was disclosed in the proxy statement. The Gypsum stock ownership of all Gypsum directors was not required to be disclosed by SEC proxy regulations, which merely required disclosure of the principal holders of voting securities, as set forth in the proxy statement (pp. 39-40).

82. There is no requirement that every detail of the contacts between Korholz and Susquehanna officers and employees through the end of April, 1965, and the negotiations which began early in May, 1965, be disclosed. None of these contacts and negotiations was material. Full information concerning the arrangement ultimately negotiated was disclosed in the proxy statement (pp. 36-37). The allegation of a transfer of control was not based on the evidence and therefore could not and should not have been disclosed. The negotiations with American Export had no bearing whatsoever on the proposed merger.

83. The capitalization table (p. 8), consolidated balance sheet (p. F-13), and notes to financial statements of Gypsum (p. F-18) were claimed to be false because they did not disclose that, as of June 30, 1965, the insurance companies allegedly required that the bank loan be paid off immediately after the merger. The proxy statement disclosed this information (p. 37):

> " * * * The insurance companies originally stipulated . . . that their consents to this transaction were con-

> ditioned upon immediate repayment of the bank loan in the event of a subsequent merger. This provision has since been eliminated and the insurance companies have agreed to an extension of the bank loan to December 31, 1966."

Thus, the proxy statement was not false or misleading in stating that, as of November, 1965, the due date of the loan from First National Bank of Boston was December 31, 1966 (p. 37), and, as of June 30, 1965, the due date was July 15, 1966 (p. F-18, n. (2)). The record establishes that this due date of July 15, 1966, was extended to December 31, 1966, prior to the mailing of the proxy material.

84. So long as the stockholders were informed that Bard's resignation was accepted July 15, 1965, (p. 37, ¶ 1(d)), it was immaterial that Bard was not in the United States on May 19, was not in communication with Bogan, and was not generally informed of what was happening. In any event, the record is clear that Korholz in effect waived any condition that Bard's resignation be submitted by May 19, 1965.

85. The proxy statement is not deficient concerning the offices held by the selling stockholders, any arrangement for at least three Susquehanna directors to resign, the alleged fact that $15 per share was over the market, the alleged prior contacts between Korholz, Boshell and Lannan, and an alleged difference in statements as to what organization or individual acquired the 430,000 shares. The positions formerly held by Lannan, Lauhoff and Wirtz are described in ¶ 1(b), p. 36 of the proxy statement, together with the resignations involved. By comparing the $15 with the market prices of stock on page 21 of the proxy statement, the fact of payment of a premium was clear. The alleged prior contacts between Korholz, Boshell and Lannan were not material. The proxy statement that Gyp-

sum formally acquired the 430,000 shares on July 2, 1965 (p. 37). Under applicable accounting regulations and practice, however, because Gypsum was to acquire the shares immediately after the end of its fiscal year ending June 30, Gypsum's independent auditors required Gypsum to show the shares as a corporate asset and the $6,450,000 bank loan as a corporate liability for fiscal year 1965. To have treated the asset and liability any differently would have constituted a misrepresentation to the stockholders of Susquehanna.

86. The information concerning Korholz' ownership of Gypsum stock not shown on pages 16-17 of the proxy statement appeared on page 40 thereof.

87. The alleged litigation against Korholz and the reasons for the evaluation of litigation in the proxy statement were fully disclosed. Admission of a conviction (p. 28) does not require description of the prison term served, if any. Not even the registration requirements of the 1953 Securities Act so provide. Prior litigation in which Korholz may have been involved was also immaterial.

88. The reasons for failure of prior merger discussions in early 1965 were not material for the purposes of the proposed merger recommended to the stockholders six months later.

89. The proxy statement is not deficient concerning disclosure of a June 18, 1965, resolution offered by Martin and Thomson which allegedly prohibited a merger between Susquehanna and a company in which an officer or director of Susquehanna had any interest. The resolution solely provided that the Acquisition Committee would be prohibited from purchasing in the future an interest in any company in which any member of the Board of Directors had an in-

terest. Korholz already had acquired the Susquehanna shares. Susquehanna acquired no Gypsum shares prior to the merger. Both Thomson and Martin supported the merger at later Board meetings.

90. The proxy statement is not deficient concerning the Coen demand (later withdrawn) for suit against the selling stockholders of Susquehanna shares, Thomson's acting as Coen's attorney, the value of the 140,000 shares as a block, or the resale to others. The demand, of course, no longer existed. Although Susquehanna had claimed in 1964 that the stock normally might be able to draw a premium, Susquehanna in 1965 could not claim such a premium from VCA or any other prospective purchaser, since Susquehanna was being forced to dispose of its VCA stock in order to avoid an imminent trial of its lawsuit with VCA. The resale of the shares by Coen was not a corporate transaction. Coen was neither an officer, director or employee of Susquehanna. The $700,000 alleged profit was disclosed in the description of the *Dasho* complaint (p. 28). The shares were offered *bona fide* by Susquehanna to VCA and other organizations. That the VCA shares were sold at $200,000 less their original cost is clearly shown on the Susquehanna consolidated balance sheet where market price and cost of those shares were described (p. F-2).

91. The proxy statement is not deficient concerning the role of the Acquisition Committee, the uncertified nature of certain financial information, the values used by New York Hanseatic (p. 4), no further information was material. The Stone & Webster recommendation, based on an independent study, clearly referred to its concurrence with Hanseatic's recommendation of an exchange value (p. 4). The alleged prior relationships between Gypsum and New York Hanseatic and Susquehanna and Stone & Webster, as well as contacts between these investment bankers and certain di-

rectors of Gypsum and Susquehanna, were not material, did not create a situation where the evaluations were suspect, and did not have to be disclosed to the stockholders.

92. There was no material omission concerning Hardin's contract and a personal option granted by Korholz to Hardin long prior to the merger between Gypsum and Susquehanna.

(a) *Personal option.* In 1962 Korholz had given Hardin such an option for approximately 69,000 shares at an exercise price of $4 per share, in order to induce Hardin to continue as an officer and director of Gypsum, Hardin also had an option for 5,000 shares under the Gypsum option plan for corporate executives. The joint proxy statement disclosed the latter company option but not the personal option from Korholz, which, under the merger, was converted into approximately 36,000 shares at an exercise price of $7.60. The personal option was not exercised until 1967. The shares received by Hardin are still held by him. Under applicable SEC proxy rules, the personal option was not material and was not required to be disclosed in the proxy statement.

(b) *Hardin Contract.* The Hardin contract was disclosed in the proxy statement (p. 38). There is no evidence whatsoever on this record that the consideration for the payment of $1,000 per month for consulting services, a reduction from the former $2,000 per month paid to him as President, was in any manner improper in view of Hardin's association with Gypsum from its incorporation.

CONCLUSIONS OF LAW

1. This court has subject matter jurisdiction over this cause of action.

2. For the purposes of this decision it is not necessary to determine whether or not plaintiffs, individually, or on behalf of the corporation have standing to bring this action. For now, it is sufficient to assume that plaintiffs have fulfilled all standing requirements.

3. None of the defendants conspired to deliver control of Susquehanna to Gypsum, or to insure a merger between Susquehanna and Gypsum, or to cause Susquehanna to acquire, through a merger with Gypsum, any shares of Susquehanna stock.

"Conspiracy involves an element of scienter." *Jack O'Donnell Chevrolet, Inc.* v. *Shankles*, 276 F. Supp. 998, 1002 (N.D. Ill. 1967). Such guilty knowledge of or participation in a concerted. prearranged unlawful plan has not been demonstrated. Nor is one party's domination of persons and corporations a sufficient predicate for finding a conspiracy existed. *Bankers Life & Casualty Co.* v. *Guarantee Reserve Life Ins. Co.*, 365 F.2d 28, 32 n. 7 (7th Cir. 1966).

4. Besides some mutual mental action, some intent, plaintiffs had to show damages to themselves and to the corporation resulting directly from an overt conspiratorial act. *Nalle* v. *Oyster*, 230 U.S. 165, 182 (1913); *Neff* v. *World Publishing Co.*, 349 F.2d 235, 257 (8th Cir. 1965); *Huey* v. *Barloga*, 277 F. Supp. 864, 871 (N.D. Ill. 1967). Plaintiffs failed to prove damages resulted from the alleged conspiracy involving the acquisition of 430,000 shares of Susquehanna stock, the change in management of Susquehanna which followed, the exchange of certain shares of VCA owned by Susquehanna for its own shares, and the merger of Susquehanna and Gypsum. No

looting of Susquehanna occurred, in violation of the common law, Section 17(a) of the Securities Act of 1933 or Sections 10(b) or 14(a) of the Securities Exchange Act of 1934, as the result of either of these transactions. Moreover, the exchange ratio for the Susquehanna-Gypsum merger was fair and equitable to the Susquehanna stockholders, did not damage either Susquehanna or its stockholders, and did not produce a violation of Section 17(a), Section 10(b) or Section 14(a).

5. As the block of stock sold to Korholz represented only about 15% of the outstanding shares of Susquehanna, no voting control of Susquehanna was transferred by the sale of 430,000 shares of Susquehanna stock to Korholz or by the resignation and replacement of four Susquehanna directors. The owners of a block of stock which may constitute working control of a corporation do not violate the common law, Section 17(a), or Section 10(b) in selling their stock at a price in excess of the market price with an agreement that working control shall immediately be transferred to the buyer by means of seriatim resignations of incumbent directors who are replaced by nominees of the buyer.

> "Even assuming that Fasco realized a premium for its controlling block, that alone would not entitle plaintiffs to relief. *Essex Universal Corp. v. Yates*, 305 F.2d 572, 576, 13 A.L.R.3d 346 (2d Cir. 1962); *Manacher v. Reynolds*, 39 Del. Ch. 401, 165 A.2d 741 (Del. Ch. 1960); see, 3 Fletcher Cyclopedia Corporations, § 900, p. 325. These cases held that a majority or controlling stockholder is under no duty to other stockholders to refrain from receiving a premium upon the sale of his stock which reflects merely the control potential of that stock. There is no obligation under such circumstances, to 'share and share alike'. . . . Control is not a corporate asset, but is rather an attribute of stock ownership.

> "Similarly, a purchaser is free to offer a premium for a block of control stock. This is so, even though control stock is purchased pursuant to a plan to acquire the remainder of the shares at a lower price, if, by private purchase or the normal economics of the marketplace, this can be achieved. It is only where fraud, deceit or manipulation enter that a violation of state law or of Rule 10b-5 occurs. . . .
>
> "Furthermore, even if it were assumed that the directors of Brown had violated their fiduciary management duties by approving the plan of acquisition, the complaint would fail to state a claim for relief under 10b-5."
>
> *Christophides* v. *Porco*, 289 F. Supp. 403, 405 (S.D. N.Y. 1968).

Absent bad faith, intent to defraud or negligence, none of which have been shown in this case, the receipt of a premium for a large block of stock is no fraud upon nonselling shareholders. *Goode* v. *Powers*, 397 P.2d 56, 59-60 (Ariz. 1964); *Benson* v. *Braun*, 155 N.Y.S. 2d 622, 627 (1956); see also *Comment*, 54 Mich. L. Rev. 399, 403 (1956). Absent fraud, neither the common law, Section 17(a), nor Section 10(b) were violated when any defendant sold his Susquehanna stock for the best price obtainable and resigned from his position on the Susquehanna Board of Directors. See *SEC* v. *Texas Gulf Sulphur*, 401 F.2d 833, 855 (2d Cir. 1968), cert. denied, 394 U.S. 976 (1969).

In the absence of proof of damages to the shareholders or the corporation, defendants are not liable under Section 10(b). *Swanson* v. *American Consumer Industries, Inc.*, 415 F.2d 1326, 1331 (7th Cir. 1969); *Globus* v. *Law Research Service, Inc.*, CCH Fed Sec L. Rep. ¶ 92, 474 (2d Cir. 1969); 98245, *Mader* v. *Armel*, 402 F.2d 158, 163 (6th Cir. 1968), cert. denied, 394 U.S. 903 (1969).

6. Accordingly, defendants J. Patrick Lannan, Howard Lauhoff, and Franklin B. Schmick committed no violation of the common law, Section 17(a) or Section 10(b) in selling their Susquehanna stock at a price in excess of the market price and resigning their positions on the Susquehanna Board of Directors. Similarly, none of the other defendants are liable under the common law, Section 17(a) or Section 10(b) for assisting in, or remaining silent with respect to such sale.

7. Directors and officers of a Delaware corporation are fiduciaries to the corporation and its stockholders. *Guth* v. *Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939). Consequently, defendants, as directors of Susquehanna, were fiduciaries, if not trustees, to the corporation and its stockholders. *Cohen* v. *Beneficial Industrial Loan Association*, 337 U.S. 541 (1949).

8. Absent a showing of bad faith, which, the court finds has not been shown, reliance by defendants as directors of Susquehanna on their informed business judgment, is a complete defense to any allegation of a breach of a director's fiduciary duty to Susquehanna or its stockholders.

> "In the absence of a showing of bad faith on the part of the directors or of a gross abuse of discretion the business judgment of the directors will not be interfered with by the courts."
> *Warshaw* v. *Calhoun*, 221 A.2d 487, 492-493 (Del. 1966).

9. Defendants, as Susquehanna directors, under applicable Delaware law, did not breach their fiduciary duty to Susquehanna's stockholders or violate Section 17(a), Section 10(b), or the common law, where, as the result of the exercise of an informed business judgment, and in the absence of bad faith, a corporate asset (VCA shares) was

exchanged on a market-to-market basis for Susquehanna shares held by dissident stockholders. See *Cheff* v. *Mathes*, 199 A.2d 548, 554 (Del. 1964); *Kors* v. *Carey*, 158 A.2d 136, 141 (Del. Ch. 1960).

10. Similarly, defendants, who exercised an informed business judgment in approving the Gypsum-Susquehanna merger, did not commit any breach of fiduciary duty or violate Section 10(b) in their management of Susquehanna.

> "The whole purpose of having such a variegated group as members of a board is to gain the benefit of their pooled experience, without expecting that each will apply identical talents and without requiring each to analyze every pertinent specialized document. Nor is there any mechanical legal requirement that the defendant directors insist upon a certain type of appraisal of valuation in determining the fairness of an offer for the purchase of the company's assets and business, provided it appears that under all circumstances they exercise reasonably prudent judgment in reaching their decision."
> *Richland* v. *Crandall*, 262 F. Supp. 538, 547 (S.D. N.Y. 1967).

Accord, *Knauff* v. *Utah Construction & Mining Co.*, 408 F.2d 958, 965 (10th Cir. 1969), cert. denied, 396 U.S. 831 (1969). *Gerstle* v. *Gamble-Skogmo, Inc.*, 298 F. Supp. 66 (E.D. N.Y. 1969) is factually distinguishable.

Lannan and Lauhoff have no legal responsibility for any acts of Susquehanna or any acts of the other defendants subsequent to May 18, 1965, the effective date of their respective resignations. Schmick has no legal responsibility for any acts of Susquehanna or any acts of other defendants subsequent to June 18, 1965, the effective date of his resignation. Such acts for which said defendants have no responsibility include the exchange of Susquehanna stock for stock of the

Vanadium Corporation of America owned by Susquehanna, the Susquehanna-Gypsum merger, and the Joint Proxy Statement distributed in connection with the merger.

11. No defendant made any material misrepresentation or omission in connection with the April 19, 1965, stockholders' meeting of Susquehanna, either prior to or at that meeting, in violation of Section 17(a), Section 10(b), or Section 14(a), or the common law.

12. Defendants timely disclosed all information required to be disclosed by Section 17(a) and Section 10(b) in connection with the sale and purchase of the 430,000 shares of Susquehanna stock. No such information, regarding the transaction, was material prior to its disclosure to the financial community.

13. There was no failure by defendants to disclose material inside information, as required by Section 17(a) and Section 10(b), with respect to the exchange of VCA shares for Susquehanna shares.

14. No material omissions or misrepresentaitons occurred in the merger proxy statement in violation of Section 10(b) or Section 14(a). Plaintiffs were fully informed of the details of which they complain before the merger was consummated.

15. Neither Susquehanna nor its stockholders were damaged by that merger.

16. The use of New York Hanseatic Corporation and Stone & Webster Service Corporation to perform certain appraisal and evaluation work in connection with the Susquehanna-Gypsum merger did not make the merger proxy statement deficient and thus did not constitute a violation of Section 17(a) or Section 10(b).

17. Any Conclusions of Law contained in the Findings of Fact are incorporated by reference herein.

Consequently, this court finds in favor of all defendants and against the individual and corporate plaintiffs. This cause is dismissed with each side bearing its own costs and attorneys fees.

ENTER:

/s/ ABRAHAM L. MAROVITZ
Abraham L. Marovitz

Date: February 6, 1970.

APPENDIX C

STATUTORY PROVISIONS INVOLVED

SECURITIES EXCHANGE ACT OF 1934

Section 10(b), 15 U.S.C. §78j(b)

§ 78j. *Manipulative and deceptive devices*

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

S.E.C. RULES

Rule 10b-5

17 C.F.R. § 240.10b-5

EMPLOYMENT OF MANIPULATIVE AND DECEPTIVE DEVICES

REG. §240.10b-5. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) to employ any device, scheme, or artifice to defraud,

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.